Crowdfunding innovative ventures in Europe
The financial ecosystem and regulatory landscape

FINAL REPORT (EN)
A study prepared for the European Commission
DG Communications Networks, Content & Technology by:
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EXECUTIVE SUMMARY

The objective of this report is to provide a state of play of the crowdfunding industry in Europe with a particular focus on equity-based crowdfunding and its regulatory aspects, providing initial concepts for self- or co-regulation of the sector.

The landscape of crowdfunding models can be grouped into two families: the non-financial return models (donation, reward or pre-selling) and the financial return models (equity or lending) which are all very different in terms of characteristics for the campaign owners and campaign backers. Europe has a scattered landscape of different models and within each model several variants exist, especially in the case of equity-based crowdfunding. The report focuses on equity-based crowdfunding on which the impact of regulation is most complex and demanding compared to the other crowdfunding models.

The global crowdfunding market has grown substantially over the past few years and a large worldwide potential for crowdinvesting is expected to materialise in the next decade. The development and growth on a national level varies widely and depends on many factors situated in the demand, supply or cultural aspects.

Equity-based crowdfunding interacts in many ways with the established financing sector as a complementary or alternative financing method in the early stage financing market. The instrument succeeds in attracting funds from non-traditional investors and a new type of business angels emerges. Not surprisingly, the traditional actors are starting to look at this form of crowdfunding as well, with business angel networks increasingly using crowdfunding-alike technology to organise their network and investment syndicates, but also with venture capital investors actively engaging on platforms. Currently, the latter group of investors still see complications for follow-on investments after a crowdfunding round, but this is starting to change.

R&D close to commercialisation can enjoy crowdfunding by attracting seed equity financing or most commonly by pre-selling products or services on a non-financial crowdfunding platform. Crowdfunding of pure R&D activities is not very popular yet and the potential for it remains to be seen.

The success factors for a crowdfunding campaign are a complex set of interdependent drivers that can be categorised into 4 main groups: the platform characteristics, the campaign characteristics, the communication efforts and the investment case (only for
Crowdfunding is a relatively new funding instrument with a highly dynamic market under continuous evolution. A few trends were identified such as the objective of established platforms to grow beyond their national borders. Secondly, most crowdfunding models are attracting the interest of well-known and trusted consumer brands who are starting to embrace this sector. Thirdly, institutionalisation of the sector, driven by traditional financial services actors, is expected. Lastly, new market segments will get challenged by crowdfunding actors, for instance the real estate sector and possibly the insurance industry.

European regulation, such as the Prospectus Directive and MiFID, provides most of the necessary building blocks for Member States to sufficiently regulate the sector. It is the Member States’ authority to translate the applicable European directives into national regulation or guidelines. The wide array of instruments in equity-based crowdfunding is driven by the differences in national regulations. Each basic type of equity-based crowdfunding comes with variants offering different rights to the investors or liabilities to the investee. Contrary to what one would expect, fundraising by the means of issuing equity directly to the investor, is not the most common financing instrument brokered on the equity-based platforms.

Some EU Member States have implemented or started to implement national regulation or guidelines specifically applicable to financial forms of crowdfunding, triggered by a developing crowdfunding scene in their country. The current national regulations, aimed at enhancing the protection of retail investors, are quite diverse and form a barrier for platforms to operate cross-border.

On a global level, other countries’ governments are also seen to develop adapted regulation to equity-based crowdfunding. The US authorities are in process of implementing a federal regulation, but delays have triggered individual states to publish intrastate regulations. Australia, which has seen an early success case of equity-based crowdfunding, has recently published a new regulation specific to equity-based crowdfunding. Japan or South Korea have similarly published or prepared regulation and also China considering regulation for equity-based crowdfunding.
A scorecard for equity-based crowdfunding could help regulatory stakeholders to monitor the market development and potentially assess the impact of new regulations over time. Four key groups of KPIs are proposed in this report: the market demand, the maturity of the regulatory framework, the supply of intermediary services and the supply of capital.

The EU institutions are taking various steps to support the development of crowdfunding as a means to spur economic growth whilst safeguarding the interests of retail investors. This report aims to contribute to this effort and reflects the views from stakeholders from within and outside the crowdfunding sector on various regulatory concepts related to the non-financial and equity-based crowdfunding models. An enhanced regulatory framework is deemed to be beneficial to all stakeholders in these segments.

Currently, limited evidence of fraud or abuse is known for the non-financial return models, as it is inherently self-regulated by the characteristics and mechanisms of the model itself. Wisdom of the crowd, a relatively short feedback cycle and the public nature are limiting the potential of fraud. A code of conduct could further enhance transparency and leverage the trust-building between the campaign backer, campaigners and the platform.

The regulatory framework for the equity-based model needs to evolve to overcome the lack of transparency and differences between markets. A quality label could serve as an effective solution to address some issues in this model whilst improving investor protection in the near term. The EU could be instrumental in providing a forum for all actors in order to achieve this objective. In addition, the growth of the market could be spurred by a cross-border harmonisation effort, potentially driven by European industry associations and national authorities.
## Abbreviations and Acronyms

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Meaning</th>
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<tr>
<td>AIFMD</td>
<td>Alternative Investment Fund Managers Directive</td>
</tr>
<tr>
<td>ASSOB</td>
<td>Australian Small Scale Offering Board</td>
</tr>
<tr>
<td>BA</td>
<td>Business Angels</td>
</tr>
<tr>
<td>CAMAC</td>
<td>Corporations and Market Advisory Committee</td>
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<tr>
<td>EBA</td>
<td>European Banking Authority</td>
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<tr>
<td>EIS</td>
<td>Enterprise Investment Schemes</td>
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<tr>
<td>ESMA</td>
<td>European Securities and Markets Authority</td>
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<td>EU</td>
<td>European Union</td>
</tr>
<tr>
<td>EuSEF</td>
<td>European Social Entrepreneurship Funds</td>
</tr>
<tr>
<td>EuVECA</td>
<td>European Venture Capital and Social Entrepreneurship Funds</td>
</tr>
<tr>
<td>EVCA</td>
<td>European Private Equity &amp; Venture Capital Association</td>
</tr>
<tr>
<td>JOBS Act</td>
<td>Jump-start Our Business Start-ups Act</td>
</tr>
<tr>
<td>MIFID</td>
<td>Markets in Financial Instruments Directive</td>
</tr>
<tr>
<td>RTD</td>
<td>Research and Technological Development</td>
</tr>
<tr>
<td>SEC</td>
<td>Securities and Exchange Commission</td>
</tr>
<tr>
<td>SEIS</td>
<td>Seed Enterprise Investment Scheme</td>
</tr>
<tr>
<td>SFA</td>
<td>Securities and Futures Act</td>
</tr>
<tr>
<td>SME</td>
<td>Small or Medium-sized Enterprise</td>
</tr>
<tr>
<td>STCP</td>
<td>SpaceTec Capital Partners</td>
</tr>
<tr>
<td>UCITSD</td>
<td>Undertakings for Collective Investment in Transferable Securities Directive</td>
</tr>
<tr>
<td>VAT</td>
<td>Value Added Tax</td>
</tr>
<tr>
<td>VC</td>
<td>Venture Capital</td>
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1. INTRODUCTION

Crowdfunding can be defined as an open appeal to the general public in order to raise funds with a specific objective. The concept itself is far from new and has been embedded in human culture since its early days. Historically, people have been raising money to achieve certain objectives for the common good. Numerous examples of charitable donation campaigns can be found in early history, however, the term crowdfunding typically denotes raising funds through the use of the Internet. The emergence of online crowdfunding dates back to more than a decade ago, but the use of a dedicated platform for several crowdfunding campaigns has only gained traction in recent years.

The development of entrepreneurship, the creation of start-ups and the growth of SMEs are considered important contributors to the economy in terms of innovation, competitiveness, employment and growth. Crowdfunding contributes to this economic growth, by generating additional revenue for companies or by providing capital to start-ups and SMEs. In addition, the social network mechanism that powers crowdfunding platforms brings together market participants who, in an offline context, would not have the opportunity to meet.

Crowdfunding brings many promising benefits that align well with the objectives of the European Commission. The Entrepreneurship 2020 Action Plan¹ aims to increase the level of employment by reinforcing entrepreneurship across Europe. It invites Member States to evaluate the need to amend national financial legislation to facilitate alternative financing, in particular the financial forms of crowdfunding. Furthermore, in the context of the European Union’s Digital Agenda for Europe, one of the seven pillars of the Europe 2020 Strategy, the European Commission emphasises innovation, entrepreneurship and competitiveness as a prerequisite for stimulating economic growth and creating employment. The European Commission is therefore aiming to strengthen support for entrepreneurs seeking to start and develop ICT businesses.

Furthermore, the European Commission held a public consultation\(^2\) on crowdfunding in the EU at the end of 2013 and subsequently published a communication on the topic.\(^3\) **This report has as its high-level objective to provide a regulatory state of play and to formulate initial concepts on how to improve the conditions of the equity-based crowdfunding ecosystem, in order to enhance access to finance for innovative start-ups and projects.** Crowdfunding can provide access to small rounds of equity as well as additional revenue via pre-selling and reward-based crowdfunding campaigns. In order to foster crowdfunding opportunities for start-ups in Europe, a dialogue between entrepreneurs, investors and crowdfunding platform operators is required. In this context, the European Commission has commissioned this study in order to analyse the current market and its trends, to provide a perspective on the international landscape and lastly, to investigate the merits and limits of self-regulation and the potential of public regulation for the equity-based model.

2014 marks a pivotal year for European equity-based crowdfunding to grow into a viable alternative funding mechanism for innovative start-ups and projects. The crowdfunding market evolved significantly over the past year; the sector is striving to professionalise itself in order to bring about expansion and to enhance credibility vis-à-vis investors. National governments are becoming increasingly aware of the potential of all types of crowdfunding and several initiatives at national and European level are being undertaken to support the industry in its development. This report aims to contribute to those efforts and to provide insights into the regulatory issues at hand for policy-makers and the industry itself.

A particular focus of this report is equity-based crowdfunding, on which the impact of regulations is the most complex and the regulatory framework is the most demanding compared to the other crowdfunding models. Secondly, great potential is evident for this model in terms of supporting young and innovative companies in Europe. It should be noted that equity-crowdfunding is currently a relatively small sub-segment in the crowdfunding market, but is expected to become an important source of finance in the venture ecosystem.

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\(^2\) European Commission, Consultation Document: Crowdfunding in the EU – Exploring the added value of potential EU action, 2013

\(^3\) European Commission, COM(2014) 172 final, Unleashing the Potential of Crowdfunding in the European Union
2. Definitions

Crowdfunding is the monetary variant of crowdsourcing. In crowdfunding, an appeal for funds is made to the general public in support of a project or company, the crowdfunding campaign. Whilst, technically speaking, crowdfunding has taken place throughout history (e.g. in the 1300s raising funds from the general public for building cathedrals and other charitable projects became remarkably successful and hence became regulated⁴), crowdfunding generally refers to raising funds or capital via the Internet on a specifically designed crowdfunding platform. Crowdfunding campaigns are at times complemented with other crowdsourcing aspects such as crowdsourcing the campaign’s acceptance on a platform, review of the business model, acquiring business advice, sourcing potential distribution channels, etc.

The crowdfunding campaign is typically conducted through a campaign page launched on an intermediary Internet platform, called the crowdfunding platform. For most crowdfunding models, a properly executed campaign entails much more than just a campaign page. The beneficiaries of the fund, the so called campaign owners or campaigners, need to maintain their campaign page to actively build an online community supporting their campaign and to engage social and other online media. Crowdfunding platforms often operate an all-or-nothing model, in which the campaign only receives funding when the full target funding amount is reached or exceeded. The people providing financial support to the campaign are called the campaign backers or sponsors, depending on whether the expected return of the campaign are monetary or not for them, they can also be called investors/lenders or donators.

⁴ Mullin, Foundations of Fundraising, 1995
3. **The Crowdfunding State of Play**

3.1. **European landscape of crowdfunding models**

The landscape of crowdfunding models in Europe is fragmented due to the regulatory differences and the cultural variances between European Union Member States. Nevertheless, two main categories of crowdfunding models can be identified based on the objectives and expectations of the crowdfunding campaign backer. For the first group of models the expected return of the campaign is **non-financial** in nature and ranges from virtually nothing to a product or service. In this case, the motives of a campaign backer can be diverse, such as the will to contribute to the common good or a desire to finalise a product or service under development. In the second group of crowdfunding models, also called crowdinvesting, the expected return is predominantly **financial**, often without any other consideration from the campaign backer other than his/her confidence in the viability of the campaigner’s business model and the projected returns.

![Figure 2: Overview of non-financial return and financial return models](image)

A particular focus of this report is to investigate those aspects of crowdfunding that impact innovation. Innovative start-ups and projects can benefit from both groups of models, although there are distinctive differences between the objectives, motives and expectations of the campaign backers. Equity-based crowdfunding in particular is expected to become an important source of capital for innovative start-ups in the future and is therefore emphasised in this report. Furthermore, the wide variety of equity-based model and the density of regulatory aspects, make the equity model of most interest in the context of this study.
The following table summarises the motives from the perspective of the campaign owners on one hand and the campaign backers on the other hand; it also highlights the advantages and disadvantages of the two groups.

<table>
<thead>
<tr>
<th>Expected return</th>
<th>Campaign owner’s perspective</th>
<th>Campaign backer’s perspective</th>
</tr>
</thead>
<tbody>
<tr>
<td>Non-financial return</td>
<td>Ranging from virtually nothing to memorabilia or a prototype/finished product depending on the size of the investment</td>
<td>+ Identification of early adopters or potential recurring customers</td>
</tr>
<tr>
<td></td>
<td></td>
<td>+ ‘Free’ market viability check and marketing</td>
</tr>
<tr>
<td></td>
<td></td>
<td>+ No equity dilution or long-term financial obligations</td>
</tr>
<tr>
<td></td>
<td></td>
<td>- No involvement of the backer as typically only funding is provided and limited feedback during the campaign</td>
</tr>
<tr>
<td>Financial return</td>
<td>Financial participation in revenue or profit, equity or interest on loans</td>
<td>+ No equity dilution in lending model or profit/revenue sharing model</td>
</tr>
<tr>
<td></td>
<td></td>
<td>+ Investing-savvy or high-net-worth individuals often interested in investing ‘publicly’ in equity campaigns</td>
</tr>
<tr>
<td></td>
<td></td>
<td>- Passive observers/investors alike non-involved BA or VC</td>
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<td></td>
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</table>

Table 1: High level pros and cons of non-financial versus financial return models

The non-financial return crowdfunding models attempt to gain support by appealing to the emotional aspects of the campaign, by highlighting its charitable aspects, by appealing to the interest or curiosity of potential backers or by creating a marketable need for the expected product or service enabled by the campaign. The return for funding the campaign differs by model:

- In the donation model the campaigner promises to execute a certain task or activity (i.e. cancer research) or h from the donation but relies on the altruistic motives of the backer (i.e. financial aid to someone in need);

- In the reward model the campaign backer promises a symbolic reward that is not proportionate to the backers funding;
In the **pre-selling model** the campaign backer promises to deliver a prototype, a finished product, or a service for a limited period of time, proportionate to the backers funding.

Apart from raising money, the key advantage for a company campaigning in this group is the opportunity to gain traction from potential customers and to receive instant feedback on whether their proposed product or service has commercial potential. Citizens willing to join crowdfunding campaigns may become the company’s first customers and grow into early adopters of the funded company’s products or services.

**Financial return crowdfunding models** offer the general public the opportunity to invest in (early-stage) start-ups or provide loans to SMEs under a variety of legal instruments. The investor expects to receive a financial return on his/her investment in exchange for accepting certain risks. The two main types of financial return models are equity and lending-based platforms. Within the **equity-based model**, a wide variety of funding mechanisms have evolved mainly to accommodate the different regulatory requirements in the Member States:

- The **profit/revenue sharing model** entitles the investor to a predefined share of the profit or revenue of the start-up or project funded during a specific period. This obligation is purely contractual and no real ownership or equity of the company is obtained;

- In the **nominee structure** a third party holds the legal titles of the equity on behalf of the crowdfunding investor who is the actual or beneficial owner. The nominee acts as the sole interface of all the crowdfunding investors towards the investee. This set-up is considered to be particularly advantageous during a subsequent financing round as it simplifies the decision process;

- Investors can obtain **direct equity** where shares are legally held by the crowdfunding investors themselves. The voting rights related to these shares differ from platform to platform;

- In the **participation model** the investor enters into a contractual obligation with a third party who then invests on behalf of all crowdfunding investors in the campaign. The legal title of the equity belongs entirely to the third party as well as any voting rights;

- **Convertible bonds** are a combination of a debt and equity instrument: the bond can be converted into equity at a predetermined conversion rate thereby
dissolving the initial debt from the balance sheet, at the moment of a follow-on financing round or exit. The main advantage of this instrument is that the valuation of the company is performed at a later stage, which is favourable for companies with high potential but uncertain future.

Crowdfunding is making investing in start-ups more accessible for the general public and is unlocking capital for those that previously did not have access to the traditional capital financing market. Many private investors are looking for alternative ways to invest as the returns on banking products are low and certain real estate markets appear over-heated. The variety of equity-based crowdfunding instruments may pose a challenge for the retail investor, as it is a complex matter for less investment-savvy individuals and because the rights of the investor differ from platform to platform and country to country. The danger of impulse buying or faddish investing exists and retail investors should be cautious in their due diligence and realistic about the risks of investing in start-ups.

The investee obtaining capital through this model has to take into account the impact of crowdfunding on the shareholder structure of the company, with future investment rounds in mind. Traditionally, professional investors investing in the later stages prefer to invest in companies with a simple shareholder structure and in which the majority of the shares are still owned by the founders who are considered to be the critical human capital of the company. The legal construct of the equity investment of the crowdfunding campaign has to be analysed in detail in order to avoid potential issues in the future financing rounds and in obtaining a fair return.

The last subset of crowdfunding instruments is the lending model, in which crowd investors, instead of a commercial bank, provide a loan to an individual (peer-to-peer lending) or company. Commercial banks are sometimes reluctant to lend money to SMEs, whereas the general public may be more willing to share the risk amongst many in order to bridge this uncertainty. The main advantage of lending for the investee is that it creates no equity dilution for the start-up’s shareholders. The return for the investor is more fixed as it is agreed ex ante that the investment is paid back by the monthly principal and interest payments throughout the lending period.

**Key Points**

- Europe has a scattered landscape of different crowdfunding models
- Each crowdfunding model has several variants, which is especially the case for equity-based platforms
3.2. Current market development

One of the first web-based crowdfunding platforms was *artistShare (US)*, launching its first campaign to raise funds for music artists in October 2003\(^5\). Europe saw the birth of the first crowdlending platform in 2005, when Zopa (UK) launched. The first crowdfunding platform to offer equity in unlisted companies to the general public is believed to be *ASSOB (AU)* in 2006.\(^6\) *Indiegogo (US)*, currently a leading crowdfunding platform, was launched at the beginning of 2008\(^7\), followed by the launch of *Kickstarter (US)* in April 2009\(^8\). The crowdfunding market has been growing substantially over the past few years, from an annual growth of 64% in 2011 to 81% in 2012. In 2013 some 600 crowdfunding platforms are forecasted to raise EUR 3.8 billion in total globally, a projection in growth of 88%.\(^9\) Today, industry experts indicate that the growth of the market is ever faster. The European market for crowdfunding is estimated at EUR 735 million in 2012, a 65% increase compared to 2011, the second largest market by funds raised.\(^9\)

![Figure 3: Global distribution by geography and type of model (M EUR)](image)

The lending model has grown the most rapidly, with a 111% increase in 2012 compared to 2011, and is expected to have become the largest crowdfunding model of 2013. The second largest growing models for 2012 are the donation/reward models which grew by 85% in 2012 compared to 2011. The equity model had a relatively low growth of 30% in 2012 compared to 2011, which can be attributed to the fact it is a relatively new model which still has a large number of regulatory hurdles to solve. The

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\(^5\) artistShare, www.artistshare.com  
\(^6\) Crowdfunding World Summit 2013, www.crowdfundingworldsummit.com/crowdfunding  
\(^7\) Indiegogo, www.indiegogo.com  
\(^8\) Kickstarter Blog, www.kickstarter.com/blog  
growth predicted for 2013 is higher, with an increase of 43% compared to 2012.\textsuperscript{9} The crowdinvesting market is expected to grow significantly across all models over the coming decade: a report by The World Bank estimates that the total crowdinvesting market potential will reach EUR 70 billion per year by 2025, excluding North America.\textsuperscript{10} In comparison with other traditional financing sources such as venture capital which amounted to EUR 36.5 billion in 2013\textsuperscript{11}, it can be concluded that crowdfunding has great potential for start-ups and established businesses across the globe, and has the prospect of becoming an alternative solution for early stage financing.

Recently, equity-based crowdfunding platforms in Europe have been extending their geographic scope and some platforms aim to operate on a pan-European level or even beyond (e.g. Seedrs (UK) allows companies from all over Europe to participate, through a UK holding company; crowdcube (UK) has a localised Spanish and Polish website; and FundedByMe (SE) has ran campaigns in SE, FI, DK, NO, EE, IT, ES, MT, UK and NL). On the investor side, business angels expect equity-based crowdfunding to provide access to quality dealflow beyond their immediate geographic reach. A similar trend can be noted in the lending model (FundingCircle (UK) expanded its operations to the US and Ratesetter (UK) to Australia).

The market development of the equity-based crowdfunding model on a national level within Europe is disparate and dependent on cultural, financial and regulatory factors.

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\textsuperscript{9} The World Bank, Crowdfunding’s Potential for the Developing World, 2013

\textsuperscript{10} Ernst & Young, Adapting and Evolving, Global venture capital insights and trends 2014, 2014
One of the main cultural factors influencing the uptake of all crowdfunding models in certain Member States is the degree of familiarity with e-commerce in general amongst the general public. In countries with low familiarity and limited user experience regarding e-commerce, online transactions are uncommon and may be met with scepticism. On average, nearly 60% of internet users\textsuperscript{12} in Europe reported they had shopped online in 2012. The highest shares of online purchases were recorded in Northern and Western Europe, whereas in Eastern and Southern Europe more traditional methods of shopping are preferred.\textsuperscript{13} The growth of equity-based crowdfunding is naturally also influenced by the demand for seed financing itself. According the Global Entrepreneurship Monitor, the availability of entrepreneurial finance for SMEs in Europe is distinct in each country, but Southern Europe is lagging behind to some degree.\textsuperscript{14} The report takes “entrepreneurial finance” to include business angels, bank loans and venture capital as well as subsidies and grants. Lack of entrepreneurial finance may not necessarily indicate a strong demand for finance. Available data suggests that the demand for online investment is high in the United Kingdom, Ireland and parts of Northern Europe (when compared with the number of start-ups per capita).\textsuperscript{15}

\footnotesize{\textsuperscript{12} The Eurostat report defines an internet user as an individual aged 16 to 74 having used the internet within the 12 months prior to the survey conducted.\textsuperscript{13} Eurostat, News Release 147/2013, 2013\textsuperscript{14} J.E. Amorós et. al., The Global Entrepreneurship Monitor 2013 Global Report, 2014\textsuperscript{15} Dataset provided by F6S, Dataset of angel.co, SpaceTec Analysis}
National regulatory frameworks can also influence market development. Nevertheless, it is considered to be too early to draw conclusions on their effect on the market. Currently, the regulatory frameworks of Northern and Western Europe are the most developed. In terms of international market development, the different national regulatory frameworks imply crowdfunding platforms must investigate the applicable regulation in each Member State, they wish to operate in. In addition, the national regulation in a number of countries requires platforms to obtain a license from the national financial authorities, which consumes significant financial and human resources of the platforms.

The United Kingdom is currently leading the equity-based crowdfunding market in Europe both in terms of number of platforms (approximately 50 platforms were identified) as in total volume of capital raised, followed by Germany and France. The United Kingdom is also spearheading the lending market in Europe, in terms of volume, value and diversity. Sweden and Finland are leading the equity-based crowdfunding market in Northern Europe and in Southern Europe Italy and Spain hold the majority of the market share. Very limited activity was identified in Eastern Europe.

![Figure 6: Density of equity crowdfunding platforms in Europe](image)

An estimate of the leading equity platforms in Europe, ranked by their total volume of capital raised until the end of 2013 and attributed to the country where the platform is based, is shown below.
An interesting example of the growth potential of equity-based crowdfunding is the case of the German crowdfunding scene, which has grown significantly over the last two years. *Innovestment* and *Seedmatch* pioneered equity-based crowdfunding market in Germany in 2011. As the largest market in the EU-28, Germany is an attractive country and several platforms have launched in recent years, including non-German platforms. Currently, *Seedmatch* accounts for half the market, followed by the more recent entrants.
The available data on the German market indicate that equity crowdfunding currently surpasses the donation/reward-based models in terms of volume, and has been growing significantly faster.

**Key Points**
- Europe is the leading region for the equity-based crowdfunding and crowdlending models
- The development and growth on a national level varies widely
- The large worldwide potential for crowdinvesting will materialise in the next decade
3.3. Positioning in the traditional financing market

Crowdfunding is a new source of finance vis-à-vis the traditional finance market for start-ups and SMEs, but its rapid emergence has generated a considerable amount of awareness within the start-up financing communities. Increasingly, interactions between equity-based crowdfunding and the traditional players are observed. Equity-based crowdfunding can come into play at different stages of the funding chain of (innovative) start-ups. For each stage a number of financial and non-financial support mechanisms and instruments already exist and the interaction of those with equity-based crowdfunding is here analysed.

![Figure 9: Crowdfunding’s activity field in the funding chain of a high-growth start-up [EUR]](image)

Insight into the market needs of start-ups with regard to online investments is available from F6S, a leading online start-up community. A noteworthy trend is the relatively high preference of North-American start-ups for convertible bonds, a preference not presently shared by their counterparts in other geographical areas.

![Figure 10: Preferred equity instrument by start-ups seeking online investment (3.000 cases) [%]](image)

Equity-based crowdfunding campaigns are commonly initiated during the incubation stage, raising capital of between EUR 50 K – 300 K. Traditional financing sources active at this stage include business angels, incubators and accelerators, with some venture capital funds also active in this stage.

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18 Dataset provided by F6S; STCP Analysis
In several regions in Europe, **business angels** form an important source of financing for start-ups, but the statistics available on angel investors are limited. Angels are private investors who provide their own capital to start-ups, generally in a sector in which they have previous professional experience. A key strength of business angels is that many of them provide ‘smart capital’, bringing valuable industry experience and a network of contact within the sector in addition to the financial support. On the downside, business angels tend to invest locally and are often acting alone. For these reasons, they are difficult to access and not necessarily aware of the market practices in the venture capital industry, which cause problems for entrepreneurs attempting to manage a diverse shareholding structure. In recent years, networks of angel investors have emerged, and in some cases equity-based crowdfunding can serve as a means to involve angels more systematically – e.g. **Angels Den (UK)** – and in this respect, business angels are a key investor group in the context of crowdfunding. A further example of the potential of crowdfunding can be found in Belgium where business angel syndicates serve as the lead investors in equity-based crowdfunding campaigns on **MyMicroInvest (BE)**. Other business angel syndicates utilise equity-based crowdfunding platforms to manage closed investment rounds for their members. Angels have attracted the attention of policy-makers as an important source for early-stage financing and in some countries the authorities have implemented measures to support this market (most notably in the United Kingdom with the SEIS and EIS incentives\(^\text{19}\), which have certainly had an considerable impact on the uptake of equity-based crowdfunding in the UK).

**Incubators and accelerators** are two business support mechanisms originating from the United States that have also gained a foothold in Europe. Incubators are well established and widespread across Europe and provide an array of support mechanisms and services, such as office space, mentoring and networking opportunities - but typically only very limited amounts of capital. Accelerators (which only emerged in the last decade, use a stringent selection process - selecting only high potential teams for short and clearly-defined period of time - and maintain close, hands-on involvement in order to improve the success rate of the participants. In addition, they differ from incubators as they provide pre-seed equity investment to start-ups. Accelerators generally focus on high-tech sectors, investing mostly in software/internet-based start-ups who have the potential to generate revenue in the

\(^{19}\) The Seed Enterprise Investment Scheme (SEIS) and Enterprise Investment Scheme (EIS) are tax incentive schemes for British individual investors to stimulate investment in higher-risk small companies in the United Kingdom
short-term. The opportunity to investment in accelerator’ funds (which subsequently invests in the programme’s start-ups - was until recently limited to the accelerator’s corporate partners, but examples of accelerators raising funds on equity-based crowdfunding platforms have emerged in recent times. Due to their focus on specific business models in specific sectors and the comparatively small size of investments, accelerators are considered to be a very limited support mechanism, despite their success. In contrast, equity-based crowdfunding is suitable to a broader range of companies and allows more capital to be raised, but obviously lacks the dedicated business mentoring available through accelerators.

<table>
<thead>
<tr>
<th>Accelerators</th>
<th>Launch date</th>
<th>Characteristics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Seedcamp</td>
<td>2007</td>
<td>Largest pan-European accelerator</td>
</tr>
<tr>
<td>Techstars London</td>
<td>2009</td>
<td>Formerly Springboard, now member of the TechStars Network</td>
</tr>
<tr>
<td>The Founder Institute</td>
<td>2009</td>
<td>US accelerator active in Europe</td>
</tr>
<tr>
<td>Startupbootcamp</td>
<td>2010</td>
<td>Accelerator coordinating the activities in five cities</td>
</tr>
<tr>
<td>Wayra</td>
<td>2011</td>
<td>Corporate accelerator of Telefonica</td>
</tr>
</tbody>
</table>

Table 2: Leading accelerators in Europe

**Debt financing** is a valuable source of financing for businesses with a lower risk profile, but innovative start-ups find access this resource difficult due to their lack of a risk/credit history and assets, and this financing source is better suited for more established SMEs. In the aftermath of the financial crisis, commercial banks have been increasingly reluctant to provide capital to SMEs. Several government incentives (generally in the form of guarantees) have been created for banks e.g. to offer long-term debt with little or no interest added to the equity raised by early stage companies. Business lending on crowdfunding platforms becomes an alternative to commercial banking especially for established SMEs and has a similar growth potential to consumer peer-to-peer lending.

Active in the seed stage and foremost in the A- and B-rounds is **venture capital**, investment funds for high-growth and early-stage companies. Even if the European venture capital industry lags behind when compared to North America, Europe has some notable success stories such as Skype, Vente Privée, CSR, and more recently, companies such as Zalando or Supercell. One of the issues for start-ups in Europe at present is the rather limited number of investments by venture capital funds in companies at the seed stage, which is critical for the generation of new businesses in Europe.
An exception is in the DACH\textsuperscript{21} region, in which the number of seed investments is relatively high compared to the European average, thanks to government seed investments. The equity-based crowdfunding platforms, mostly active in the incubation and seed stages, could be considered as an extremely valuable solution to this issue and stimulus to promote entrepreneurship in Europe. Furthermore, examples of venture capital investments being made on those crowdfunding platforms alongside investments from the general public have recently emerged. Most noteworthy amongst these is the recent financing round of \textit{crowdcube} (itself an equity-based crowdfunding platform), which raised GBP 1.2 million from the crowd together with GBP 3.8 million from Balderton Capital. Another example is Future Ad Labs, which at present has raised nearly GBP 500 K of which GBP 90 K from Passion Capital.\textsuperscript{22}

\begin{figure}[h]
\centering
\includegraphics[width=\textwidth]{figure11}
\caption{Number of companies funded by venture capital in 2011\textsuperscript{20}}
\end{figure}

\begin{figure}[h]
\centering
\includegraphics[width=\textwidth]{figure12}
\caption{Early Stage Investment in Europe in 2013 [\%]\textsuperscript{22}}
\end{figure}

\textsuperscript{20} EVCA / PEREP Analytics
\textsuperscript{21} Germany, Austria and Switzerland
\textsuperscript{22} EBAN, Early Stage Investment in 2013, www.eban.org/angel-investment-grows-to-e5-5-billion, 2014; EVCA, 2014
When comparing the amount raised on equity-based crowdfunding platforms with business angels and venture capital for early stage companies, it can be concluded that this model of crowdfunding is quite small. Nevertheless it is expected that equity-based crowdfunding will grow significantly over the coming decade and will become an important source of capital in the financing landscape.

Case Study

The average crowdcube campaign (UK)\(^ \text{23} \)

crowdcube is a leading European platform active in the United Kingdom offering direct equity deals to its members. The characteristics of an average deal on the platform mid 2013 were:

<table>
<thead>
<tr>
<th>Characteristic</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average investment raised</td>
<td>EUR 212 K</td>
</tr>
<tr>
<td>Average investment per member</td>
<td>EUR 2,956</td>
</tr>
<tr>
<td>Average equity offered</td>
<td>16 %</td>
</tr>
<tr>
<td>Average number of investors</td>
<td>71</td>
</tr>
<tr>
<td>Average deal length</td>
<td>45 days</td>
</tr>
</tbody>
</table>

Since the publication of these statistics, larger deals have taken place on the platform, it is therefore expected that the average investment raised will have increased.

Key Points

- Crowdfunding is a complementary source of finance, interacting in many ways with the established financing sector
- Equity-based crowdfunding becomes an truly alternative financing method in the early stage financing of young companies
- New types of business angels emerge and equity-based crowdfunding succeeds to attract funds from non-traditional investors
- Business angel networks are starting to look at equity-based crowdfunding as a means to organise themselves
- Currently, venture capital investors still see complications for follow-on investments after an equity-based crowdfunding round, but this is starting to change
- There are first signs of venture capital investors actively engaging on equity-based platforms, helping to shape the supply market

\(^\text{23}\) Crowdcube, www.crowdcube.com
3.4. Potential for innovation

Innovative projects or start-ups typically require a certain amount of research and technological development (RTD) effort to be made in order to develop technologies and to subsequently commercialise them into an end-product or service. Many examples of successful crowdfunding campaigns have proven that this type of financing is feasible for RTD projects and start-ups. Smaller campaigns aimed at supporting basic research can also be found, although their appeal is more limited, since the end-result of the campaign and the reward for the campaign backer are not likely to be as tangible and immediate as in RTD campaigns. Apart from the obvious financial benefit, crowdfunding offers campaign owners the added benefit of increased awareness of, and engagement with, the campaign’s subject matter. Furthermore, crowdfunding has a much lighter administrative burden and is more flexible (not being dependent on funding cycles and research topics) than traditional public funding instruments for RTD.

<table>
<thead>
<tr>
<th>Crowdfunding model</th>
<th>Ideal types of innovative project or start-up</th>
</tr>
</thead>
<tbody>
<tr>
<td>Donation / Reward</td>
<td>Innovative campaigns to the benefit of the common good, consisting of RTD or basic research aspects</td>
</tr>
<tr>
<td>Pre-selling</td>
<td>Innovative campaigns requiring a well-defined volume of RTD funds to develop technology and to commercialise it into a compelling end-product, which can be pre-sold to the campaign backers</td>
</tr>
<tr>
<td>Equity</td>
<td>Innovative campaigns which require an estimated amount of RTD efforts which may result in a commercial product or service for which a sizeable market potential exists, although the campaign does not aim to sell its products or services to investors themselves</td>
</tr>
<tr>
<td>Lending</td>
<td>Crowdlending is not very well suited for innovative start-ups nor medium to high risk R&amp;D projects.</td>
</tr>
</tbody>
</table>

Table 3: Ideal types of innovative project or start-up by crowdfunding model

Innovative campaigns on crowdfunding platforms can raise funds in two ways: either by generating additional income for the project or start-up on donation/reward platforms, or by raising capital on equity platforms. Whilst campaign owners are not restricted in regard to the type of crowdfunding they use to raise funds, the above table indicates the ideal match from a theoretical point of view. Entrepreneurs are most likely to benefit from the pre-selling model, where revenue generated from the campaign funds the commercialisation phase of a product design or the development of a service. Pure research and development at a low maturity level (i.e. no prototype exists) lends itself best to the donation or reward model, where the outcome of the
campaign is the effort itself rather than a tangible result to be delivered to the campaign backer.

The Oculus Rift case study highlights the complexity of the relationship between a campaign and its backers, and stresses the importance of informing the crowd of the mechanisms in some of the crowdfunding models.

### Case Study: Oculus Rift (USA)


Oculus used crowdfunding to build its Oculus Rift Developer Kit - a virtual reality headset - and the company raised USD 2.4 million from a campaign on Kickstarter (US) during the summer of 2012. While the Oculus had a working prototype, additional funding was required to develop and manufacture the Developer Kit. The company attracted the attention of the public after it had been taken over for USD 2 billion by Facebook. Many of the campaign backers were disappointed that they did not receive a share of the profits it made from the take-over. As Kickstarter is a reward-based/pre-selling platform, it is only natural that the campaign backers were not entitled to the revenues associated with the acquisition, but many backers felt wronged. The company received quite negative publicity from some of its backers, which was counterproductive to the community engagement it had previously attained. It can be argued that in this case equity crowdfunding might have been a more suitable platform as the investors in the campaign would have benefited from the subsequent financial success of the company. On the other hand, Oculus did not have much choice at the time, as equity crowdfunding was not quite established yet in 2012 and it did have a product to pre-sell. Furthermore, the successful campaign on Kickstarter, which raised nearly 1000% of its original goal, generated a great deal of publicity for its product. It also provided a sound market validation, which has influenced the take-over price; something that may have not been achieved if funds had been raised on an equity platform.

Some donation/reward crowdfunding platforms have a specific focus on funding basic research or RTD, however, the amounts raised on these platforms are currently small when compared to the total crowdfunding market. The most prominent examples are:

- **Experiment (US)**: a donation-based platform which aims to fund selected scientific research projects varying from basic to applied research (EUR 794 K raised to date)

- **Petridish.org (US)**: a reward-based platform for funding scientific research, the platform currently has no ongoing campaigns (EUR 112 K raised to date)

- **Technofunding (UK)**: a reward-based platform designed to fund mostly technology-related research and projects (EUR 2.3 K raised to date)

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- **#SciFund Challenge (US)**: this platform acts as an intermediary in the sense that it supports scientists in preparing research proposals, which are then crowd funded in waves on a third-party crowdfunding platform (EUR 232 K raised to date)
- **FundaGeek (US)**: this reward-based platform focused on funding inventions and more specifically software development, but it ceased operations in 2013

Other donation/reward-based platforms might not have a specific focus on RTD, however, some of the campaigns funded on those platforms certainly contributing to innovation. Technology-related campaigns, a proxy for RTD projects, are not the core business of the leading crowdfunding platforms globally: technology represents only 2.2% of the successfully funded campaigns on **Kickstarter (US)**, where the vast majority of campaigns are related to creative industries such as music, film, art, publishing and theatre. Furthermore technology campaigns are underperforming compared to the average campaign on these platforms. It should be noted that the success rates of **Indiegogo (US)** in the figure below only give a rough indication of its overall performance, as **Indiegogo** automatically delists unsuccessful campaigns raising less than USD 500.

![Figure 13: Success rate of average campaign vs. technology campaigns](image)

Equity-based platforms include a much higher percentage of technology-related campaigns (i.e. 31% of the campaigns on **crowdcube (UK)** are categorised as technology-related) than the donation/reward platforms. This could be partly explained by the fact that start-ups in the technology sector are typically more aware or accustomed to raising funds through venture capital. The total number of projects and amounts raised, however, is still only a fraction of those on the non-financial

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25 Jonathan Lau and Edward Junprung, docs.google.com/spreadsheet/ccc?key=0AobjVQ7EKnjldGpGYWg1WE1BVZHtktuRkFkWW9QbGc#gid=2 (last retrieved June 2014)
return platforms. Nevertheless, this strongly indicates the potential of equity-based platforms for innovative start-ups.

Key Points

- Pure R&D is not yet popular on crowdfunding, its potential remains to be seen.
- R&D that is close to commercialisation can be funded in a traditional way by attracting seed financing or by pre-selling on a non-financial crowdfunding market.
- Proof of concept and proof of market is a key advantage of pre-selling crowdfunding and will be increasingly provided by this instrument.
3.5. Success factors for crowdfunding

The crowd’s decision on whether or not to support a crowdfunding campaign is very much based on emotion and as such, the time spent by a potential backer in reading the details of a crowdfunding campaign and subsequently deciding whether or not to contribute is only a matter of a few minutes. Surprisingly, this also holds true for crowdinvesting. Therefore it is evident that campaign owners must take great care in developing their campaign page and related documents in order to maximise the success rate of their campaigns and to engage the crowd effectively using all available technological means. Central to the decision-making process is the concept or idea for which the campaign is raising funds, which needs to have sufficient traction with the crowd in order to be successful. The campaign objectives have to be compelling and engaging for the general public or the target audience of the campaign.

![Diagram: Success factors crowdfunding campaigns](image)

*Figure 14: Success factors crowdfunding campaigns*

The key components of a successful campaign are the communication, the platform, the characteristics of the campaign itself and the investment case (for the equity and lending campaigns), whilst it should be noted that for lending-based platforms mostly the latter will come into play. The platform chosen by the campaign owner has to suit the needs of the campaign and to foster its success. The crowdfunding model operated by the platform, needs to properly reflect the financial interests of the campaigner as

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27 Interviews with industry experts
well as those of the potential campaign backer. A criterion for the campaign owner might be the overall volume raised by a platform (whether or not in the specific market relevant to the campaign). Whilst a platform’s overall raised volume might be significantly lower than the leading platforms, its specific market focus might contribute more to the campaign’s fundraising success. Lastly, the geographical focus of the campaign should match the geographical focus of the platform in order to enhance success. Furthermore, research indicates the geography of the campaign owner itself may also come into play\textsuperscript{28}.

A second set of success factors revolves around the ability of the campaigners to communicate effectively in order to capture the engagement of the potential campaign backers in a short amount of time. Driving traffic to the campaign is a prerequisite: utilising the campaigners’ personal network, further extended by social media are one of the first steps towards the campaign’s success. A marketing strategy must be devised, as the campaign’s duration is very limited in comparison with other fundraising efforts and the optimal usage and planning of the campaigners’ resources is also key to its success. For larger campaigns, it is essential to generate traction in the professional media, online and offline, in order to drive visitors to the campaign. Subsequently, to convert the page visitors into campaign backers, the campaign page on the crowdfunding platform should look professional and feature appealing multimedia. According to the platform owners interviewed, the most effective way to communicate the idea is an attractive video of the campaign. In addition, the campaign’s content and objectives should be clear and understandable to a wide audience, highlighting how the raised funds will be used. After the campaign’s launch, the campaign owners should build an active community, by posting regular updates on their campaign page and by responding to the feedback, suggestions and concerns raised by interested members of the community.

Other decisive factors for the campaign’s success naturally include the characteristics of the campaign itself. The team’s composition and their credentials play a role, especially for larger campaigns, as conveying trust is of the essence in any type of fundraising. As already indicated in the previous section, the market sector of the campaign influences the success rate of the campaign. Data from the world’s leading crowdfunding platform Kickstarter, indicates a high success rate for some areas of the arts sector whereas technology is relatively underperforming, however, the specialised

\textsuperscript{28} E. Mollick, The dynamics of crowdfunding: an exploratory study, 2013
platforms or platforms with different models obtain different success rates per sector. Contrary to what might be assumed, research indicates that the duration of a campaign limits its success, as a longer campaign duration might signal a lack of confidence from the campaigner\(^{29}\). An analysis of successful campaigns in the technology sector seems to suggest that the attractiveness of the offered reward is an important driver for the success of the campaign. Similarly for the donation-based models, the success of a campaign is dependent on the perceived benefit to the common good or emotional appeal. Lastly, campaigns containing a novelty factor are more likely to attract attention on social and professional media, driving more traffic to the campaign page. A famed example is the Potato Salad campaign on Kickstarter, which raised more than USD 50 K in order for the campaigner to simply make a potato salad\(^{30}\).

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**Case Study**

**DNAdigest (UK)\(^{31}\)**

- **DNAdigest** is a non-profit organisation based in the UK, which has as objective to promote and facilitate publishing and sharing of genomic data to the benefit of research.
- DNAdigest launched a donation crowdfunding campaign on Thunderclap with the goal of raising USD 25 K to organise public events.
- The campaign stranded at little over USD 5 K and the start-up analysed why they failed:
  - The key message of the campaign was not properly conveyed and was too difficult
  - The campaign did not reach out to major press or media outlets in their audience nor did they have a back-up plan for when it went wrong
  - The start-up did not have the necessary human resources available to fully support the promotion of the campaign
- **DNAdigest did not see the underfunding as a complete failure**, the campaign still helped to attract industry sponsors and the support of the community.

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One set of factors which is only relevant for the business-oriented equity/lending-based platforms is the **investment business case** of the campaign. Similarly to the investment analysis performed by the traditional finance providers, the business model, projected financials, market potential and exit opportunities play a role in the investment decision. It should be noted, however, that the due diligence conducted by online investors on equity-based platforms is on average far more superficial than

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\(^{29}\) E. Mollick, The dynamics of crowdfunding: an exploratory study, 2013

\(^{30}\) Kickstarter Potato Salad campaign,

\(^{31}\) Interview; DNA Digest Website
those of the traditional financing actors and the decision process is more based on instinctive buy.

Lastly, it should be noted that successful campaigns become even more attractive and successful due to the herd instinct: if a certain number of individuals make a decision, it becomes more likely that others will do the same. This social behaviour highlights the necessity to launch a campaign with as many success factors as possible fulfilled from the start.

**Key Points**

- Success factors are a complex set of interdependent drivers that can be categorised into 4 main groups: platform characteristics, campaign characteristics, communication and investment case
- A recipe for building a successful campaign does not exist, however, committing sufficient resources to enable as many success factors as possible will certainly increase the likelihood of success
3.6. A perspective on future trends

Crowdfunding is a relatively young funding instrument under continuous evolution which provides an alternative to the traditional funding chain. Many stakeholders from both within as well as outside the sector have been interviewed to identify ongoing and future trends. Whilst it is challenging to forecast how this industry will evolve in the coming years, the authors of this report have consolidated the views of industry experts and have evaluated the following hypotheses with input from many stakeholders.

A growing number of platforms started to operate across borders in 2013 marking the start of the internationalisation of the crowdfunding platforms. It is expected that this trend will accelerate further, as it is driven by the need to increase economies of scale and to expand the platforms’ eco-systems both in terms of the campaign influx and the campaign backers’ donation/investment volume. One of the barriers for internationalisation is differences between the regulatory frameworks in each EU Member State and the need for a localised approach. Nevertheless, a few European champions are overcoming this issue and are increasingly expanding their offering to several countries. The interviewed platforms believe that the emergence of non-European platforms in the European market is only a moderate threat, as localisation is essential for success in Europe and domestic platforms naturally maintain a local social network and connection to their respective communities.

For all types of crowdfunding models, it is expected that the smaller platforms will become more specialised in order to differentiate themselves from the leading generalist platforms. The most successful ways for platforms to differentiate themselves could be driven by a very strong local (geographical) focus, or by strengthening the platforms’ offering through the inclusion of crowdsourcing of non-financial elements specific to their niche market alongside the fundraising mechanism. An example of this specialisation can be found on the platform Seed&Spark (US) which focuses entirely on the independent movie industry, offering not only its donation funding instrument but also the possibility for the crowd to lend movie production materials to the film maker.

In the medium-term the consolidation of the crowdfunding industry is anticipated especially for the equity and lending-based platforms, with the leading platforms acquiring the most interesting campaigns and investors, driving competitors with smaller platforms out of the market. The increasing momentum of the
internationalisation of these platforms is deemed to fuel this trend in the medium-term.

There are a few examples of innovative companies that maintain closed crowdfunding-like platforms on their organisation’s intranet, in order to spur internal innovation and technological development. **Enterprise crowdfunding** offers the opportunity for employees to submit internally innovative ideas and to donate their allocation of company funds to the campaign of their liking. A notable example is IBM which is believed to be one of the first companies to have run several successful crowdfunding pilots. Each employee was assigned an allotment that could be pledged to projects of other employees on IBM’s internal crowdfunding platform. It reversed the decision-making process from top-down to bottom-up and it was found to be much more time efficient compared to using other innovation platforms. An added benefit was excellent inter-departmental collaboration and the initiation of many new working relations.

Companies, universities and not-for-profit organisations are seen launching dedicated crowdfunding platforms on existing third-party platforms or even their own website, using white-label or proprietary technology. External **Do-It-Yourself crowdfunding** showcases the company’s commitment to social responsibility, leveraging the online traffic from their corporate website to enhance the success of crowdfunding campaigns, but first and foremost it serves as an excellent marketing tool. Large online web platforms, such as online market places, might have a financial interest in setting up a crowdfunding platforms themselves in the future, diversifying their business. Universities have no immediate commercial intentions but aim to generate funds for their own research projects and to help their spin-off companies in attracting funding.

A trend that has recently started to emerge and is expected to expand significantly in the near future is the **institutionalisation of the equity and lending-based platforms**, in terms of both the users of the platform and investors in the platforms itself. Recently, a number of venture capitalists have started to invest in campaigns on equity platforms alongside the crowd to enlarge their dealflow. These platforms are actively trying to engage venture capitalists, as well as business angels. Equity crowdfunding will play an important role for existing business angels as platforms take over the process and paperwork from the business angel networks and allow individual

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Crowdfunding is a new and highly dynamic sector with under continuous evolution.
Increasingly, established crowdfunding platforms are looking to grow abroad.
Well-known and trusted brands are starting to embrace this sector.
Institutionalisation of the sector can be driven by traditional financial services actors.
New market segments will gradually be challenged by crowdfunding actors, for instance the real estate sector or possibly the insurance industry.
4. **Analysis of the Regulatory Status Quo**

4.1. **European perspective**

4.1.1. European regulatory framework

The operations of all crowdfunding models are potentially subject to different European regulations. The *Payment Services Directive*\(^{34}\) may have an impact on all crowdfunding models, as most platforms manage funds of campaign backers in one way or another. The directive provides the legal foundation for the creation of an EU-wide single market for payments, with the objective to make cross-border payments as easy, efficient and secure as national payments within a Member State. Crowdfunding platforms often manage the process of handling the monetary commitment of the campaign backers in the timeframe between a backers’ commitment and the actual completion of the campaign. Platforms often use a third-party payment provider in order to comply with respective regulatory requirements. If funds are reclaimable in the event of a failed (non-funded) campaign, then the platform may also require a license as a credit institution according to certain interpretations of the Directive. This situation arises specifically if a campaign fails and investors can choose between reclaiming funds and allocating funds to another project, in contrast to the situation of an automatic reimbursement. Both the upfront deposit of funds into a virtual account, or funds that need to be reallocated after failed campaigns, could effectively be classified as electronically storing funds to be used for payment transactions, and could require that the crowdfunding platform is licensed as a credit institution.

Publicly soliciting investments or the act of public offering is regulated by the *Prospectus Directive*\(^{35}\). The Directive harmonises the drawing up, approval and distribution of the prospectus when securities are being offered to the public in the EU. The objective of the directive is to ensure investor protection and market efficiency, next to contributing to a single European financial market. The Prospectus Directive offers the freedom to national legislative bodies to implement a country-specific financial promotion regime between certain financial thresholds, at which the

\(^{34}\) Directive 2007/64/EC

\(^{35}\) Directive 2003/71/EC
Directive ceases to apply. Promotions that fall outside the scope of the Prospectus Directive’s definition can therefore still fall under the scope of national regulations. The Prospectus Directive contains a harmonised exemption for offerings that do not exceed EUR 100 K, individual Member States have the autonomy to implement a country-specific regime for offerings that are above EUR 100 K up to EUR 5 million. Naturally, many different national regimes between the EU-wide exempted threshold of EUR 100 K and the EU-wide harmonised full prospectus regime above EUR 5 million have been developed. If one was to launch an offering in all EU countries that stays exempted from the requirement to draw up a prospectus, the offering would have to be below EUR 100k, because only the EUR 100 K exemption applies on a cross-border, Europe-wide basis. To avoid the obligation and associated costs to prepare a prospectus, some platforms designed transactions to remain outside the scope of the national implementation of the Prospectus Directive, or its definition of securities.

<table>
<thead>
<tr>
<th>EU Directive</th>
<th>Equity</th>
<th>Lending</th>
<th>Donation / Reward</th>
</tr>
</thead>
<tbody>
<tr>
<td>Payment Services</td>
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<td>✓</td>
</tr>
<tr>
<td>Consumer Rights</td>
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<td>✓</td>
<td>✓</td>
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<tr>
<td>Anti-Money Laundering</td>
<td>✓</td>
<td></td>
<td>✓</td>
</tr>
<tr>
<td>Distance Marketing of Financial</td>
<td>✓</td>
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<td></td>
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<tr>
<td>Services</td>
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<td>Prospectus</td>
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<td>Capital Requirements</td>
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<tr>
<td>UCITSD</td>
<td>(✓)</td>
<td></td>
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</tr>
</tbody>
</table>

Table 4: Overview of European legislation and its applicability to crowdfunding models

For lending-based crowdfunding, the act of deposit-taking for consequent credit-granting may be considered as a regulated banking activity under the Capital Requirements Directive. Different operative models are possible: the crowdfunding platform is not always the party that collects the funds, nor is it necessarily the party that will ultimately provide the loan directly to the project holder. Members may make transactions with each other directly, peer-to-peer, which is then merely facilitated or

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36 ✓ = Likely to be applicable to most business models; (✓) = Would be applicable only in very specific circumstances
37 Directive 2013/36/EU
brokered through a platform but the platform operator itself does not act as a party. Some countries may adopt an interpretation where this does not require a license - although other countries may require a license for such credit intermediation. Furthermore, regulations regarding consumer loans may play a role; these originate under the Consumer Credit Directive\textsuperscript{38}. The directive aims to ensure that all consumers in the EU enjoy a high and equivalent level of protection of their interests and to create a genuine internal market.

Equity platforms rarely operate a passive-facilitating model where members can make direct transactions without any legal involvement from the platform operator, but instead are often involved in the transaction as a party. Acquiring an equity stake in a company often entails that a number of requirements have to be met under the respective company laws of the relevant Member States, foremost to protect the existing shareholders of the company. These company laws naturally influence the organisation of equity crowdfunding platforms and the legal framework they operate in. Start-ups generally opt to become incorporated as private companies, as they initially do not need to adopt more complex and hence more expensive company structures. Entities that are created under the European Private Company regime and under national company laws are often bound to limitations when engaging new and unknown investors. These limitations may take the form of specific formalities in the event of an equity increase, such as notarised shareholder resolutions/subscriptions, or the need for qualified majorities when taking votes or when accepting new shareholders. In some Member States it is more difficult to accept equity investments from third parties that do not belong to the existing stakeholders, rules designed to prevent a company from diluting the value of existing shareholders or their voting rights. In some Member States platforms found alternative ways for firms to fundraise by issuing equity-like instruments: contracts are offered with pay-offs that are similar to the financial return that would have been gained by an equity investment. Other options include to fund structures via an intermediate special-purpose vehicle or to use a nominee structure.

European legislation regarding investment services and in particular the Markets in Financial Instruments Directive (MiFID)\textsuperscript{39} can also be a factor that shapes the organisation of crowdfunding platforms. This directive’s aim is to improve the competitiveness of EU financial markets by creating a single market for investment

\textsuperscript{38} Directive 2008/48/EC
\textsuperscript{39} Directive 2004/39/EC
services and activities, and by ensuring a high degree of harmonised protection for investors in financial instruments. Nevertheless, MiFID does not cover all forms of crowdfunding as not all instruments of the different investment crowdfunding models are negotiable and fall under the scope of MiFID as transferable securities. Stakes in private firms may not be negotiable and may not be considered as a MiFID regulated activity – units in private firms are often expressly excluded from negotiability. Loans are not financial instruments that fall within the scope of MiFID.

Where the crowdfunding instrument falls within the scope of MiFID, the platform’s activities can qualify as a MiFID investment services/activities in one of the following respects:

- Investment advice;
- The placing of financial instruments;
- The execution of orders on behalf of clients;
- The receipt and the transmission of the order in relation to one or more financial instruments;
- Operating a multilateral trading facility;
- Operating an organised trading facility (MiFID II);
- Services related to underwriting.

While certain crowdfunding activities may fall within the scope of MiFID, it should be appreciated that this legislation predates the take-off in crowdfunding activity. Therefore the applicability to crowdfunding of this directive and its transposition into national legislation may in some cases not be easily apparent to firms and regulators and different judgments may be made. In areas where MiFID does not apply or is not maximally harmonised, member states may in addition adopt their own approach to regulating crowdfunding. As discussed above, there are significant cultural differences across European jurisdictions which lead to the adoption of different business models, to which MiFID will apply in different ways.

In practice, platforms are often not subject to the MiFID regime, and often do not have an incentive to apply to for MiFID authorisation if they do not intend to operate on a cross-border basis under the MiFID European passport. Nevertheless, unless national or European law provides otherwise, crowdfunding not regulated under MiFID, may mean the platforms are exempt from e.g. client classification, one of the investor protection measures of MiFID.
Some equity crowdfunding platforms adopt the approach holding the equity in the investee through an intermediate holding vehicle after a successful campaign. This approach can fall under the scope of the regulations on collective investment undertakings, as it may take a fund-like format. Platforms that do not offer redemption possibilities do not fall under the scope of the Undertakings for Collective Investment in Transferable Securities Directive (UCITS)\textsuperscript{40}. Therefore, they do not have to comply with the investment restrictions as laid down in the UCITSD. They could, however, fall within the broad definition of being an alternative investment fund within the scope of the Alternative Investment Fund Managers Directive (AIFMD)\textsuperscript{41}. This Directive includes all fund structures unless they are regulated under the UCITS directive. Similarly, these funds could fall under one of the existing optional regimes provided for within the European Venture Capital and Social Entrepreneurship Funds (EuVECA) Regulations\textsuperscript{42} and the European Social Entrepreneurship Funds (EuSEF) Regulations\textsuperscript{43}. Furthermore, despite the very inclusive nature, and the wide scope of the AIFMD Directive, it only applies when exceeding high thresholds of several millions of euros, which are too high to apply to crowdfunding platforms. These high thresholds relate to the rationale behind the AIFMD Directive which is aimed at professional investors. Below these thresholds the AIFMD foresees a lighter minimum regulatory regime that may be complemented by more restrictive national rules. In addition, a platform is generally not being regarded as an alternative investment fund manager, as it will not manage the investments being made by the investors. The platform only makes a pre-selection, whereas the investors usually decide by themselves in which projects to invest or not. The AIFMD allows Member States to regulate funds at national level, and to decide whether alternative investment funds can be marketed to retail investors. Lastly, the Directive on Consumer Rights\textsuperscript{44}, which aims at achieving a real business-to-consumer (B2C) internal market, striking the right balance between a high level of consumer protection and the competitiveness of enterprises; the Distance Marketing of Financial Services Directive\textsuperscript{45}, which establishes and harmonises principles relating to financial services which may be provided at a distance offering better protection for any consumer negotiating or entering into a contract with a supplier established in

\begin{footnotesize}
\begin{itemize}
\item \textsuperscript{40} Directive 2001/107/EC and Directive 2001/108/EC
\item \textsuperscript{41} Directive 2011/61/EU
\item \textsuperscript{42} Regulation (EU) No 345/2013
\item \textsuperscript{43} Regulation (EU) No 346/2013
\item \textsuperscript{44} Directive 2011/83/EC
\item \textsuperscript{45} Directive 2002/65/EC
\end{itemize}
\end{footnotesize}
another Member State; and the *Anti-Money Laundering Directive*\(^\text{46}\) could also impact the operations of crowdfunding platforms.

### Key Points

- European regulation provides most of the necessary building blocks for Member States to sufficiently regulate the sector
- It is the Member States’ authority to translate European directives into national guidelines or regulation
- The main European directives applicable to equity-based crowdfunding are the Prospectus Directive and MiFID

### 4.1.2. Regulatory aspects of equity crowdfunding models

From a legal perspective two large families of platforms can be recognised: firstly those that are passive and that facilitate direct transactions between members, and secondly, those where the platform operator takes a role as a legally recognised party in the relationship, with a transaction often engineered in such a way that is compliant with regulatory or legal limitations whilst avoiding certain regulatory difficulties e.g. by taking advantage of foreseen exemptions. The equity-based platforms usually try to adapt themselves in order to conform to the least demanding legal requirements. As a result investors do not always receive direct equity in these instances, but rather equity-like contractual instruments.

In the case of equity-based crowdfunding, three platform types can be identified:

- Facilitating the sale of direct equity (possibly through a nominee structure) or loans and contracts directly between its members;
- Offering securities in an intermediate vehicle (especially the case in equity-based crowdfunding);
- Selling investment contracts like synthetic loans or other contracts that mimic aspects of loans and equity (profit-/revenue sharing, participation model, convertible bonds).

\(^\text{46}\) Directive 2005/60/EC
Only a few platforms offer **direct equity** in companies in Europe, for example, crowdcube (UK) and FundedByMe (SE). Less restrictive elements in national company laws allow these platforms to operate such a model: selling direct equity in private limited companies in the United Kingdom requires fewer formal transactions than in other countries. Similarly, in Sweden, private companies are allowed to sell direct equity if the subscription or purchase is limited to 200 people.48

Some equity models are transaction-engineered, but use neither a fund-like approach, nor a contractual approach. These equity models try to establish a direct link between investors and campaigners as far as possible. For example, Seedrs (UK) offers direct equity but this is done through a **nominee structure**. By appointing Seedrs as a nominee shareholder for every investor that invests through the platform, the challenge of dealing with a multitude of investors is solved. The nominee has a contractual relationship with the investee, and this allows the nominee to be accepted into a private limited company. This also facilitates the dealings with investors as there is legally only one counterparty/investor, similarly to an indirect model with intermediate vehicles. Nominee structures are a very common practice in the United Kingdom, however, in many other countries the concept is much less recognised.

Quite popular amongst the platforms is the use of intermediate holding vehicles, either campaign-specific special purpose vehicles or either one pooled vehicle for all campaigns that raise funds through a certain platform. In the latter case, the equity-based crowdfunding platform thereafter often distributes investment contracts (that mimic equity) to investors rather than equity, as otherwise the returns per company could not be fairly channelled to the investors that pledged for that company.

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47 SpaceTec Capital Partners Analysis

48 Note: This is an exemption to the rule that Swedish private limited liability companies and their shareholders are not allowed to attempt, through advertising, to distribute their shares or subscription rights in the company or debentures or option certificates that are issued by limited companies.
WiSEED (FR) uses the participation model which sells equity in an intermediate holding vehicle. In order to stay under the legal thresholds of the national prospectus (or similar promotion) regimes, it only supports fundraising campaigns of up to EUR 100 K, funded by fewer than 150 non-qualified investors. The continued management of the investment potentially makes the holding vehicle subject to collective investment management rules – a domain that is not yet harmonised and that requires country-specific rules under the new AIFM Directive.

The platform Symbid (NL) is another user of this model which sells units in an intermediate vehicle. The difficulty of selling equity to the public, without having to comply with notarial procedures, is solved by using a project-specific cooperative. The cooperative is a very liberal form of a company in the Netherlands and has the advantage that membership capital can easily be increased or decreased without many formalities. Cooperative members do not need to have a dual capacity unlike many other cooperative regimes in different countries (i.e. being both user and producer, or user and investor, etc.) – purely financial investors can be accepted as members. Lastly, cooperative membership units are tax transparent in The Netherlands.

MyMicroInvest (BE) which serves mainly Belgian companies but also had activity in France, illustrates the participation model which sells contracts in an intermediate holding vehicle. In principle, Belgian private companies require a substantial number of formalities that cannot be undertaken online when capital is raised. To circumvent these formalities, the platform also uses an indirect model where users actually buy stakes in an intermediate holding company, which adequately complies with the regulations that enable its stakes to be sold to the public (i.e. prospectuses are published). Nevertheless, creating a project-specific holding company is costly and therefore one single holding company is used for multiple projects. If that holding company was to sell its shares, this would create a problem for every new project that it adds to its portfolio – as the returns from that specific portfolio company would have to be channelled to the specific investors that invested for that company. It is legally impossible to attribute the pay-off of one particular project to a particular class of shares and therefore contracts that mimic the pay-off structure of shares are used. Since the intermediate vehicle itself is ultimately the counterpart for every stream of funding raised, it is required to issue a prospectus for each campaign due to the combined size of the vehicle.
A contractual *revenue-sharing model, which emulates straight equity properties*, is participation through a silent partnership with the investee (directly, not via an intermediate platform-operated vehicle). *Innovestments (DE)* is a crowdfunding platform which uses the notion of silent partnerships. In some countries these are not considered as securities and can therefore fall under the exemption of some regulations.\(^49\) In many countries, there is no common or widely used interpretation available for this case and this would lead to legal uncertainty when scaling this transaction model across borders. The contractual nature of this transaction model does not require an intermediate vehicle or compulsory nominee arrangement between the investor and the investee. *Companisto (DE)* and *Seedmatch (DE)* are platforms that originally followed the silent partnership model, but switched to a subordinated debt model, which simulates straight equity properties as well in the form of a profit-sharing contractual loan.

*Angel.me (BE)* is a Belgian crowdfunding platform inspired by the *Sonicangel (BE)* crowdfunding platform which has operated for some years under a *pure revenue sharing model* (direct, not via an intermediate platform-operated vehicle). Revenue sharing can be agreed upon contractually and it offers the advantage over shares as it can be designed in a way that it is automatically cancelled after a number of years or after a number of pay-offs. This solves the problem that equity (in the form of shares) usually faces: namely the need for a secondary market if an investor wants to derive immediate value from it. Revenue sharing contracts have a long history in industries like mining and movie production. Nevertheless, they also have an inconsistency in fiscal terms, as they can either qualify as interest payments or as dividend payments. Especially in a cross-border setting, it is not unusual that one fiscal administration may consider it as a dividend payment and another one as an interest payment. This can lead either to double taxation or to double non-taxation.

*Convertible loans* are also emerging on some platforms. During the lending period, the loan will be converted to equity in a secondary transaction in case the company receives new capital, e.g. either during a follow-on financing round or an IPO, delaying the need for a valuation of the company. In case the company did not undergo a second financing round, the principal amount of the loan is due at the end of the lending period. Convertibles offer investors the comfortable repayment options of a

\(^49\) Note: for example promotion or prospectus regimes, often due to the argument that they are purely contractual and therefore not transferable, while transferability is a condition for falling under the scope of some prospectus regimes, and certainly to fall under the scope of the Prospectus Directive.
loan, but investors still participate in the upside if a company’s shares have climbed in value and if a secondary transaction is possible (as the instruments will then be converted to equity). As these are contractual instruments, rather than stakes that may be bound by restrictions under company law, the direct peer-to-peer set-up between backers and campaigners is feasible and does not necessarily require further engineering with an intermediate vehicle – although this may be possible.

**Key Points**
- Each basic type of equity-based crowdfunding comes with variants offering different rights to the investors or liabilities to the investee
- The wide array of instruments in equity-based crowdfunding is driven by differences in national regulations
- Direct equity is rarely brokered through equity-based platforms

4.1.3. National regulatory framework

Some countries, like France, Spain and Italy are either working on, or have published, crowdfunding-specific regulations in the past two years, typically requiring to obtain a registration or a license and to comply with a number of specific requirements. Such requirements reflect the best practices that are found in any regulations regarding financial activities and aim to provide a layer of protection for the investor. They include e.g. fit and proper person requirements for those that perform a management function, minimum capital requirements and a proper internal organisational structure within the crowdfunding platform’s business. In addition, crowdfunding-specific regulations greatly increase the legal certainty for platform operators. Non-compliance is sanctioned. Nevertheless, even without such specific regulations, crowdfunding platforms are often already subject to similar requirements that have their origins in more general regulations for the financial services sector.
Figure 16: Intensity of national regulatory efforts for equity crowdfunding in EU-28

France

In France, the different types of crowdfunding mechanisms could be easily interpreted as implicitly providing regulated services under France’s implementation of the European Payment Services Directive and Electronic Money Directive. Cooperating with a partner who holds a suitable license from the national authorities usually exempts the crowdfunding platform itself from obtaining a license. Besides that compliance strategy, France has also introduced a light license to e-commerce operators that accept reclaimable funds or any funds that can otherwise be interpreted to fall under those regulations and equity-based crowdfunding platforms can enjoy a specific license that also includes limited permission to process payments. Nonetheless, platforms that perform lending activities and that act as a party in the credit operations between the members, require a full banking license. For platforms that merely provide financial intermediation in France, interpretations that put platforms under regulated regimes are used, under the country’s implementation of MiFID. Most French platforms do therefore hold a (limited) license. France recently also introduced a limited license for those that provide advice in the context of crowdfunding (thus, for those that operate a platform), through the adoption of the regulation ‘Ordonnance n° 2014-559’ on 30 May 2014. Disclosure is the cornerstone of this recently published crowdfunding-specific regulation, driven by the general idea that investors in crowdfunding are generally unsophisticated. Therefore, France has put an emphasis on transparency regarding the costs, and the risks.

Rules regarding the public offering of securities are, however, relatively liberal in France. In France, raising less than EUR 5 million in equity capital (but no more than
50% of the capital of the issuer) would not require a prospectus to be published. This is of course only relevant for the types of public companies that can sell shares to the public. But even for private company types, where platforms can work around the issues, the recent crowdfunding-specific regulation introduced a light prospectus regime for public solicitations of up to EUR 1 million that take place via regulated crowdfunding platforms.

As a result of this situation where licenses are generally required, but where interpretations and license requirements are straightforward, France has a relatively active equity-based crowdfunding market. Examples of platforms are Wiseed, Anaxago, Babyloan, KissKissBankBank and Finance Utile.

**Germany**

In Germany contractual equity-based crowdfunding models are relatively common and contracts are directly established between backers and project managers. Such contracts are usually stakes in silent partnerships, subordinated debt or convertible debt. Silent partnership stakes are economically similar to equity, but legally meet the definition of a contractual instrument, and not a security or an equity instrument under company law. Examples of platforms under this principle are Innovestments and Companisto. These platforms facilitate the creation of investment contracts between their members, and rely on dominant legal interpretations and exemptions that the brokerage of such investment contracts are not an activity that would require a license. This is in contrast to the brokerage of securities (shares) in firms, instead of contracts, or the lending models where the platform would be a party in the credit operations. These would actually require a license. As a result, most platforms in Germany stick to the model of brokering in investment contracts, without the need for a license. Still there are platforms like Bergfürst which opted for the regulated route and that can offer direct equity.

Until recently, the dominant use of contractual instruments used exemptions to the rules regarding public offerings. These regulate public offerings of securities, as soon as they exceed the Europe-wide exemption of EUR 100 K. Germany generally has a very strong public promotion regime. Nevertheless, in order for those rules on public offerings to apply, the offering needs to fall under the definitions of securities. These definitions include transferable securities that are negotiable on the capital markets. Stakes in German private companies and in German partnerships are not, however, seen as securities. The same is true for subordinated debt or other contractual
Nevertheless, Germany has recently published a regulatory proposal to toughen the supervision of the grey capital market. This frames in an action plan of the government to protect consumers in the financial markets. The regulations relates to mezzanine products, and some of the models that are used by equity-based crowdfunding platforms – those will then become exempt to prospectus requirements as long as the fundraising does not exceed EUR 1 million and a single contributor can invest a maximum of EUR 10 K, albeit a small information document will be necessary. The platforms will also face some rules of conduct under the proposed legislation: staff that handles investment projects will for instance need to demonstrate relevant skills. Platforms will also have to produce an information document regarding their platform itself, unless the platform accepts only contributions less than EUR 250.

**United Kingdom**
The United Kingdom lacks specific regulation for equity-based crowdfunding. The British regulator has nonetheless extensively communicated their views on crowdfunding. Equity-based platforms are generally considered to operate within the requirements for regulated activities. Even if some platforms have claimed that they operated an exempted activity, the regulator’s policy has put most equity platforms under a regulated regime now. Lending platforms could operate an unregulated activity more easily because lending-based crowdfunding was perceived to be less risky than equity-based crowdfunding, however, recent clarification on the policy suggests a trend towards more regulation of this model as well.

In the past, the United Kingdom had a very country-specific regime to regulate the promotion of investment opportunities to the public. It was also a regime that was much more inclusive than the public offering rules from the EU Prospectus Directive. For offerings where the EU Prospectus Directive gives Member States the freedom to implement their own regulations (i.e. offerings of less than EUR 5 million), the UK does even not impose a prospectus. Every promotion in this domain is thus fully regulated by the UK regulation on financial promotions (much broader than just regulating offerings). This UK-specific promotion regime is restrictive and, in principle, requires that a promotion should be approved by a licensed entity. Otherwise it only allows the promotion of equity offerings to particular categories of investors, such as professional clients, high-net-worth individuals or certified or self-certified sophisticated investors – although this self-certification possibility serves as a mechanism to broaden the restrictive nature. The regulator in the United Kingdom has published its intention to update its perspective on the promotion regulation by setting out the limits on the
types of investors a particular platform may deal with; and by offering more possibilities to promote their platforms to ordinary retail investors. The latter includes two new categories of investors: retail clients who invest on the basis of an investment advisory or management service, and retail clients that certify that they have not invested/will not invest more than 10% of their net assets, excluding their primary residence, pensions and life insurance, in unlisted share or debt securities over the 12-month periods before and after the investment.

If an intermediate vehicle was used in the United Kingdom to facilitate the transactions between investors and investees – very common in other countries – a restrictive country-specific regime on “collective investments” would apply. The platforms generally choose to avoid this regulation and this model altogether.

The UK approach has ensured that existing regulations such as MiFID are applied to crowdfunding wherever possible and the UK has a vibrant crowdfunding market, where platforms obtain a license and investor protection is ensured.

Spain

Spain did generally not interpret equity-based crowdfunding platforms as activities that require a license. Spain has a liberal regime as public offerings of investments do not need a prospectus as long as it is not above the EUR 5 million threshold prescribed by the EU Prospectus Directive. A crowdfunding-specific law is now being prepared, however, with a number of protective measures for investors and required disclosures. For instance, platforms will have to inform users about the risks associated with investing. Spain also proposes caps on contributions that individuals can allocate to crowdfunding projects, to limit their exposure to losses. The cap of EUR 3 K per project is in discussion, with the additional limitation that a single platform may not collect more than EUR 10 K through various projects per investor during a 12-month period.

As equity investments are most prone to losses, the Spanish legal initiative proposes that for equity platforms a stricter regime should apply including accounting and auditing requirements. They will also have more obligations in terms of providing information to their users (to inform and educate them about the risks). The marketing for the platforms’ campaigns will have to be strictly done through the platform and make it a controlled environment once the new regulations comes into force. In summary, equity-based crowdfunding platforms will have to:

- Fulfil a number of accounting, auditing and other prerequisites;
- Inform users about investment risks;
- Restrict marketing their campaigns exclusively to their platform.

**Italy**

Until recently Italian platforms in the equity and lending domain could avoid being regulated if they acted only as an intermediary between their members, but not as a party themselves. Public offerings are not burdened by strong rules as Italy originally excluded offerings below EUR 2.5 million (over a 12-month period) from the obligation to produce a prospectus. Recently Italy implemented a specific “crowdfunding law” to regulate this domain. It is in particularly applicable to the equity platforms, which are now required to be compliant with a number of criteria in order to be included in a dedicated register.

These criteria do not fundamentally differ from those that are normally required for intermediaries operating in the financial markets (credit institutions and investment firms) and include for example proof of the ability of the platform operator to assess the business plans submitted by investees, from an economic and financial point of view. The detailed list of requirements for platform operators further includes the need to provide mandatory information regarding the risks associated with investing in young firms (i.e. loss of capital, illiquidity, unlikelihood of dividends, dilution, need for diversification), the obligation to inform investors about a cooling down period and the practical steps that need to be taken in order to exercise this right. Platforms also need to inform members how and when information on the status of campaign will be delivered to them. Platforms further need to be transparent on the fees and costs that may be charged to investors. Furthermore, a number of typical consumer protection rules are included: these require the platform to mention the applicable law and the competent court by which the relationship with the user will be bound. Retail investors must demonstrate that they understand the nature of the activity of the portal, the nature of equity instruments and the risks associated with these. This basically boils down to completing questionnaire, similar to a MiFID investor profiling.

A very specific stipulation is that only innovative start-ups can use equity-based crowdfunding portals and the start-up may not have been active for a period longer than 48 months before starting the campaign. In addition, the company’s turnover cannot exceed EUR 5 million p.a., and the company cannot have distributed dividends in the past. Besides being a start-up, the activity of the company must be in the domain of the development and commercialisation of innovative products or services.
with high technological value. There is also a separate sub-category of the innovative start-up for social purposes. Ordinary established businesses can therefore not use crowdfunding to sell their equity. Besides the need for an innovative activities, there are a number of additional criteria that must be fulfilled in order to meet the eligibility requirements.

Before the equity offer can be promoted through an equity crowdfunding platform, 5% of the equity offer is required to be taken up by either professional investors (for instance a venture capital fund), a credit institution, a financial institution for innovation and development or by an incubator.

The advantage of this Italian legal initiative is that it eliminates uncertainty regarding a potential classification under the traditional broker-dealer classification and assures that not the full traditional MiFID procedure applies. It is too early to assess the impact of the Italian regulatory initiative.

**Northern Europe**

In the countries of Northern Europe, regulations regarding payment services are generally interpreted as not applicable to activities where compensation is provided. Also regulations regarding investment activities are rarely considered to apply to equity or lending platforms. One reason is that investment advice (a regulated activity used as a hook in some countries to bring platforms under the scope of regulations) does not include giving general recommendations to a larger group of people through the use of mass media and internet platforms. This is not a general statement, as individual countries (e.g. Sweden) still require a license when securities or investment products are sold. With regard to public offerings, in all Nordic countries promotions of up to EUR 1 million do not require a prospectus.

**Eastern Europe**

In Eastern European countries so far no dedicated crowdfunding-specific legislative interpretations have been developed. The regulators tend to place platforms under a general regulated regime. This may be under general regulated regimes for investment service providers and credit institutions. The uncertainty regarding interpretations results from an underdeveloped market of equity-based crowdfunding platforms in most countries. Nevertheless, in some countries that offer a more definitive interpretation or a more liberal setting, a number of crowdfunding platforms have emerged which operate without a license.
Regarding public solicitation, Eastern European countries vary considerably, from very liberal regimes to very restrictive regimes. In Poland for instance, situations which do not fall under the EU Prospectus Directive are also exempted from the requirement to prepare, approve and publish a prospectus under national laws. In Slovakia, there is the possibility to use and register a country-specific but simplified prospectus for such offerings. This prospectus for equity must contain the following information: details of the issuer, amount of the issuance, denomination of the shares, the rights that they offer, and information (financial and non-financial) that should allow investors to make a suitable assessment. Bulgaria as a contrasting example requires a prospectus for every public offering of securities (unless the harmonised exemption from the EU Prospectus Directive is met for offerings below EUR 100 K).

**Key Points**

- The national regulations applicable to equity-based crowdfunding are quite diverse and form a barrier for platforms to operate cross-border
- Some Member States have implemented regulation or publish guidelines in order to increase investor protection and to regulate the platforms’ operations
- Markets with a developing crowdfunding scene often trigger regulatory activity in Member States
- UK and NL financial authorities have published policy guidelines to complement the existing regulation on equity-based crowdfunding
- FR and IT have emitted new regulation adapted to equity-based crowdfunding, DE and ES are preparing new regulation
- Other Member States are researching the topic or have not yet seen the need for a specific crowdfunding regulation
4.2. International perspective

A clear and transparent legal framework for equity-based crowdfunding could be supportive to unlock the market. Globally, three categories of maturity in terms of equity crowdfunding regulation can be distinguished:

- Initial regulatory framework for equity-based crowdfunding – Western European countries and several US states;
- Regulatory framework for equity-based crowdfunding in preparation – Several European countries, US Federal laws, Australia and Eastern Asia;
- Limited or no adapted regulatory framework – Eastern Europe, Russia, Africa and South America.

Most prominently, the US JOBS Act and the subsequent discussion about its implementation by the SEC, as well as the preparation and implementation of regulation in other non-European countries, could provide a range of different perspectives for policy makers on how to approach its own regulatory efforts and to analyse how the industry and the market demand react to the different regulatory approaches.

United States

Today, the United States (US) is the largest crowdfunding market in the world. US donation/reward-based crowdfunding platforms such as *Indiegogo* and *Kickstarter* are leading globally and have paved the way for others. The US crowdfunding volumes grew strongly: in 2012, the market grew by 105%, compared to 65% growth in Europe.\(^{50}\) Europe is leading in equity crowdfunding, however, as the current US legislation does not allow securities to be issued to the general public. Only donation, reward and debt-based platforms thrived, whilst access to equity platforms is currently limited to high-net-worth individuals.

In April 2012, President Obama signed the Jumpstart Our Business Start-ups Act (JOBS Act), a regulation aimed at enhancing venture investments in the US. Title III of the JOBS Act is entirely dedicated to regulating equity crowdfunding and marked the opening of equity crowdfunding to the general public. In October 2013, following a 10-month delay, the U.S. Securities and Exchange Commission (SEC) published its

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proposed rules for comment; the final rules are expected to be published in the second half of 2014. The most important proposed rules in Title III are:\(^51\):

- A company can raise securities up to a maximum of USD 1 million (EUR 750 K) per 12-month period;
- An investor earning or having a net worth less than USD 100 K (EUR 75 K) can invest up to a maximum of USD 2 K (EUR 1.5 K) or 5% of his annual income or net worth per 12-month period\(^52\) (whichever is the greater amount);
- An investor earning or having a net worth of more than USD 100 K (EUR 75 K) can invest up to total maximum of 10% of his annual income per 12-month period;
- A company must disclose financial statements and, depending on the size of the equity-based campaign, have them certified by the principal executive officer, reviewed by a public accountant or audited by an external auditor;
- Equity-based crowdfunding platforms need to be registered with the SEC as a broker or funding platform.

The rules proposed by the SEC were perceived as too costly and burdensome by many industry actors, and as failing to make small investment easier. The main changes proposed are to increase the fundraising limit from USD 1 million (EUR 750 K) to USD 5 million (EUR 3.7 million) and secondly, to remove the obligation of (expensive) external audits for campaigns raising under USD 3 million (EUR 2.2 million). On the other hand, other industry experts support the proposed rules, arguing that the external audits for smaller companies are not as cumbersome and expensive as suggested by the critics.

Due to the SEC’s 10-month long delay in publishing the proposed rules and the following contested proposal, several US states decided to create and implement their own intrastate regulations rather than waiting for the federal implementation of the SEC’s final rules. The equity-based crowdfunding regulations in the respective US states typically increase the campaign’s limit from USD 1 million (EUR 750 K) to USD 2 million (EUR 1.5 million), fix the investor’s investment cap to USD 10 K (EUR 7.5 K) and lift the obligation for external audits. These measures aim to make equity crowdfunding less complicated and less expensive than under the federal proposal. To date, 14 states have active crowdfunding regulations and another 13 have legislation in progress. It is important to note that these intrastate regulations are only

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\(^51\) US Congress, JOBS Act, 2012

\(^52\) Note: the limit in Title III is formulated ambiguously, the SEC rules proposed would refer to ‘an investor earning and having a net worth less than USD 100 K’.
applicable within the state itself and platforms operating under these regulations are not allowed to accept investments from residents of other states.

Figure 17: Status of intrastate equity crowdfunding regulations, July 2014

Australia

The crowdfunding market in Australia is peculiar and rather different from other countries. Whilst around the world several equity-based platforms share the local market, the Australian Small Scale Offering Board (ASSOB) has taken the vast majority of the market in Australia. The platform was founded as early as 2005 and has raised AUD 140 million (EUR 100 million) since its launch, making it one of the largest equity crowdfunding platforms in the world in terms of capital volume raised.

No specific equity crowdfunding regulations in Australia existed in 2005, nevertheless ASSOB took advantage of the 2002 exemption ASIC Class Order (CO 02/273). The main restrictions were: the issuer’s fundraising limit of AUD 5 million (EUR 3.5 million) per 12-month period; and most importantly, the limit of 20 unaccredited investors being allowed to invest in a given company within a 12-month period. ASSOB

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53 Crowdfunding Legal Hub, crowdfundinglegalhub.com/2014/06/25/state-of-the-states-list-of-current-active-and-proposed-intrastate-exemptions (last retrieved July 2014); STCP Analysis
overcame this limitation by accepting only the 20 highest investment offers at the end of the campaign.\(^{56}\)

Nevertheless, as the demand for equity crowdfunding regulation increased, the Australian government had to react. In May 2014, the Corporations and Market Advisory Committee (CAMAC) published a new legal regulation\(^{57,58}\) focused solely on equity crowdfunding.

The main improvement for platform owners, is that the limit of 20 investors has been lifted, which finally opens up equity crowdfunding to the general public in Australia. The issuer’s limit remains set at AUD 5 million (EUR 3.5 million) per 12-month period under the new regulation and the investor’s limit has been set to AUD 2.5 K (EUR 1.8 K) per issuer and AUD 10 K (EUR 7 K) in total per 12-month period.

The development of the new regulation has unlocked the market, spurring the emergence of new platforms in Australia, some of them being created even whilst the new regulation was being prepared.

**Middle East**

Equity crowdfunding is slowly emerging in the Middle East and has clear potential in this region, due to its cultural and legislative environment. In the Islamic world, Sharia law influences everyday life in as well as the financial markets: issuing debt with an interest rate is prohibited in Islamic culture, however, sharing risk and profit in return for equity is perfectly feasible from a religious point of view, thus potentially providing a fruitful ground for crowdfunding. There is a strong preference for investing in ways to create an economic impact, rather than focusing solely on profit\(^{59}\). The legal framework for equity crowdfunding specifically is still undeveloped in the region. The absence of a clear regulatory scheme together with certain cultural differences seem to be the main barriers to the development of equity crowdfunding in the Middle East, but it is nevertheless assumed that the region could become a major actor in the near future. Currently the existing platforms work under general regulations for Venture Capital investments. To date no equity crowdfunding regulation laws have been created anywhere in the region.

\(^{56}\) VentureBeat, venturebeat.com/2014/01/22/crowdfunding-assob (last retrieved July 2014)
\(^{57}\) Australian Government, CAMAC, Crowd Sourced Equity Funding Report, 2014
\(^{58}\) Australian Government, CAMAC, Guide to the Crowd Sourced Equity Funding Report, 2014
Eureeca (AE) is the first equity crowdfunding platform with a focus on the Middle East. Most of its projects are in the United Arab Emirates and Jordan, although it has a few projects in other countries, such as Kuwait or Lebanon. The UK-based platform, crowdcube, started to expand to the MENA market as well in 2013.

Asia

Equity-based crowdfunding attracted attention in Asia after the JOBS Act was signed in the US in 2012. Currently there are no specific crowdfunding regulations in the region; nevertheless, several countries are in various stages of developing and implementing specific crowdfunding regulations.

Japan published a proposed regulation in May 2014, which will come into effect at the end of May 2015 after the implementation of any required amendments. The maximum amount of capital that can be raised is expected to be JPY 100 million (EUR 730 K) per campaign and a limit of JPY 500K (EUR 3.7 K) per individual investor. An essential part of the regulation is that all data must be transparent and that investors should be educated about the risks involved. Since offering securities to the general public is prohibited in Japan at the moment, there are currently no equity-based platforms. The new regulation is expected to open up the market and to unlock parts of the large capital resources in the country.

China is seeking to explore different possibilities for their approach to equity crowdfunding and may create a market larger than that of the US. As equity crowdfunding is currently illegal, China attempted a pilot project, in which investors could invest into several cultural projects with an expected annual return of 7%. China is currently considering to adopt a specific regulation for equity-based crowdfunding. While there are currently over 30 non-equity based crowdfunding platforms, the equity model is expected to grow rapidly once the relevant regulation is approved.

The law in Singapore does not specifically address the status of equity crowdfunding and it is unclear whether this violates the Singaporean Securities and Futures Act (SFA), which regulates the issue of securities. SFA has made an exemption for offerings up to

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60 Crowdcube, www.crowdcube.me (last retrieved June 2014)
SGD 5 Million (EUR 3 million) in a 12-month period if not advertised.\textsuperscript{65} As equity-based crowdfunding platforms require users to register before access is obtained, it could be considered as a closed members’ area and thus not as advertising. The Swedish platform \textit{FundedByMe} recently launched in Singapore. Nevertheless without the new regulation, which will not be implemented in the near future, the current legal situation is unclear and there is a preference for platforms to operate on the reward-based model instead.

South Korea recognises the great potential of equity-based crowdfunding. As South Korea is now focused on the so-called “creative economy”, crowdfunding is considered as an innovative way to support SME start-ups. As 80\% of people are employed by SMEs, the potential for the labour market seems very promising.\textsuperscript{66} Two proposed regulations were prepared by the SME Department and the Financial Regulator for SMEs at the end of 2013.\textsuperscript{67} Although the new regulation has not yet been finalised, the government supports the idea, and the first equity crowdfunding platform, \textit{Opportune}, is already operating in South Korea.

\textbf{Key Points}

\begin{itemize}
  \item The US authorities are in process of implementing a federal regulation, but delays have triggered individual states to publish intrastate regulation
  \item ASSOB has been active for nearly a decade in Australia. The AU government has recently published new regulation specific to equity-based crowdfunding
  \item Equity-based crowdfunding regulation in the Middle East has not yet been implemented, however, platforms are emerging
  \item In Asia, CN has started a pilot project. The regulatory situation is very diverse, JP and KR have published or are in process of implementing specific regulation
\end{itemize}

\textsuperscript{65} Insight Legal Asia, insightlegalasia.com/blog/crowdfunding-equity-based-asia-pacific-legal-and-regulatory-ambiguities-without-analogous-us (last retrieved June 2014)
\textsuperscript{67} Crowdfunding in Korea, Seong H., UC Berkeley Symposium, October 17, 2013
4.3. The taxation dimension of crowdfunding

All parties in the crowdfunding process are potentially subject to different forms of taxation during and after the campaign. The specific taxation is highly dependent on the crowdfunding model\textsuperscript{68} used and is therefore a complex matter that should be assessed on a case-by-case basis. In general, the following taxation aspects need to be considered:

- Income tax for individuals;
- Corporate tax for the parties represented by a legal entity;
- Value added tax;
- Tax deductibility for the campaign owner;
- Tax deductibility for the campaign backer.

Campaign owners should be aware of the status of their fundraising campaign for income tax (in the case of an individual or group of individuals) or corporate tax (in cases where the campaign is run by a corporation). As a general rule, income or corporate tax is due by the campaign owner for the revenue generated by a donation or reward campaigns. Under certain circumstances, it may be possible in some countries to deduct a number of costs, or to separate out the donation component to reduce the taxable base. Even campaigns generating only a one-off income and entailing a high donation component may still be taxable under the relevant national income tax regime for individuals. The tax on donations is highly country-specific and is an aspect that requires special attention from the campaign owner.

The sale of equity and debt does not constitute taxable income for the campaign owners. Proceeds from contracts that mimic equity may, however, under some national tax laws constitute taxable income. For the campaign backers themselves the taxation of dividends, interest income or revenue/profit shares will depend on the countries’ tax systems (i.e. they can be partially or fully taxable). Lastly, in case an equity campaign defaults, many countries offer tax relief whereby the losses on equity can be partially offset against other taxable income.

Crowdfunding campaigns may be subject to value added tax (VAT). The contributions made by campaign backers in a reward or pre-selling crowdfunding campaign may be seen as advanced payments in exchange for goods or services, taxable under VAT.

\textsuperscript{68} Note: for more information about crowdfunding models, refer to section 3.1
regulations. If it is considered that an economic activity is being carried out, the campaign owner pledging for money may be regarded as a taxable person, even in the case of an individual. Certain VAT provisions may still apply, such as the special scheme for small enterprises, whereby small firms can rely on an exemption to register for VAT purposes as long as their turnover stays under certain limits (e.g. GBP 79 K for UK-based firms); similarly individuals may be exempt for smaller amounts. The VAT treatment of equity-based crowdfunding may be uncertain: although transactions concerning securities are exempt from VAT, most equity crowdfunding actually relies on equity-like contracts, which could be subject to VAT. The VAT liabilities of the crowdfunding platforms themselves, which stem from the services provided to the campaign owners, should also be taken into account: the consideration that platforms receive (often a percentage of the pledge instead of a fixed fee) may be subject to VAT charges.

**Tax deductibility for the campaign backer** during the crowdfunding process is a complex matter. Corporate campaign backers in reward and donation-based crowdfunding schemes may be able to deduct the ‘purchase’ from their taxable income, in cases where the reward-based crowdfunding is related to the business of the campaign backer. The deductibility of donations by individuals in donation-based crowdfunding may be possible depending on the national regulations and some countries may require the campaign to be managed by a recognised charity. In the case of a reward-based platform, there may still be a donation component, but whether this expense will then still be deductible as a donation to a charity will depend on the national tax laws. For instance, in the United Kingdom, this depends on the value of the reward: the reward component must be 25% or less of the full donation amount and the value of the reward cannot exceed GBP 25. Lastly, an investment on an equity or lending platform may be partly tax deductible, as some countries provide tax incentives for investing in the seed stage, some including additional tax breaks in case the investment defaults.

**Tax deductibility for the campaign owner** is dependent on the specific crowdfunding model used. Concerning financial return models, the payment of dividends, interests or percentages of revenues/profits that are offered to contractual investors are treated differently in terms of tax deductibility. Dividends are paid out after corporate tax has been paid, while interest and royalty payments are considered business expenses. Nonetheless, in case of individual campaign owners instead of businesses, the interest payment may not be deductible from their taxable income base.
Crowdfunding model | Campaign owner | Campaign backer
--- | --- | ---
**Equity** | Proceeds from selling equity do not constitute taxable income. Dividends are paid out after the due corporate tax and are not deductible business expenses | Investing in equity is generally not tax deductible, but incentives may exist to stimulate seed investment which in addition may allow setting off the losses against other taxable income. The income from dividends is taxed

**Equity-like contracts and revenue sharing** | Proceeds from selling investment contracts may or may not constitute taxable income. The payments of the interest or revenue/profit shares may be considered as a business expense | Subscribing to the investment product is not deductible. Receiving a share of revenue or interest may be taxable income

**Lending** | Taking on debt is normally not taxable. The interests paid out are considered business expenses | Subscribing to the loan is not deductible. The received interests may be taxable income. Losses from bad debts can potentially be offset against gains in some countries

**Reward/pre-selling** | The net gain, after deduction of costs, is potentially taxable as business income or considered income tax for individuals | Normally not deductible (unless the reward is bought for business purposes)

**Donation** | Potentially taxable, registered charities may be able to avoid taxation of donations | Potentially deductible: member states often have an allowance to deduct donations to recognised charities from the taxable base

Table 5: Taxation aspects per crowdfunding model

- Investors and investees should consider tax implications of crowdfunding, especially when operating cross-border
- Most crowdfunding platforms are mere service providers, subject to local VAT
- The tax incentive scheme for investors (SEIS/EIS) in the UK create an additional demand effect and enhance the growth of equity-based crowdfunding
4.4. Monitoring crowdfunding from a regulatory angle

Equity-based crowdfunding is a relatively new fundraising method, its acceptance and development is very different in each Member State. There are several factors which influence the overall equity-based crowdfunding climate in a country. Regular monitoring and benchmarking of these factors could help to understand the mechanics of the market and the comparison over time can show the development directions in the different Member States and serve as a basis for monitoring from a regulatory angle with a wide EU perspective. This monitor could support the policy development and derived open publications such as presentations for conferences, newsletters, etc. support the knowledge-building and educational responsibility of the actors involved.

Figure 18: Conceptual framework for crowdfunding monitoring

Four main enabling factors influence friendliness to equity-based crowdfunding in the Member States: market demand, maturity of the regulatory framework, supply of intermediary services and supply of capital. The level of development of each of them influences the general crowdfunding climate in the country:
Market demand
The demand of innovative companies and projects for finance via crowdfunding is a key driver for the crowdfunding market development and an associated legislative pull. This demand itself is influenced by the awareness, general knowledge and acceptance of crowdfunding as a financing source by the entrepreneurs.

Maturity of the regulatory framework
Crowdfunding and most prominently equity crowdfunding is a relatively new model of fund-raising. Many of the platforms still operate in an unclear legal space as either the legal frameworks have only recently been adapted or no specific legislation exists. Each country faces the same problem of how to adapt its legislation to enable the growth of crowdfunding whilst ensuring protection of the general public. The creation of clear regulatory framework is essential for the market to unlock its potential. From this point-of-view crowdfunding friendliness can be interpreted as to which extent a Member State has taken actions to ensure clarity on its regulatory framework. It is recommended that the benchmarking exercise contains a qualitative assessment of the legal framework in each Member State, from the perspectives of campaigners, backers and platforms alike.

Supply of intermediary services
The number of platforms which intermediate between campaigners and backers, influences the competition and indirectly the quality of the market. In a developed market increased specialisation on concrete types of projects (i.e. arts, applications, energy or real estate) and subsequently a higher success rate for the campaigns can be expected. In well-developed markets it is easier to choose the most appropriate platform for a given campaign as well as to find projects focused onto investors’ interest, making the crowdfunding process more fruitful.

Supply of capital
The amount of available investable money in the country determines to some extent how difficult it will be for campaigns to raise the targeted funding. With higher supplies of capital, the percentage of successful projects will be higher and therefore equity-based crowdfunding will be recognised increasingly as a way to raise funds. Additional enabler are the ability to attract investors internationally and the familiarity with e-commerce in general.
Several indicators proposed for the analysis of equity-based crowdfunding climate can be derived from external sources. Combining these data in a quantitative and qualitative manner in regular crowdfunding scorecards can provide an overall picture about economic and regulatory situation of market, which is determining the opportunities offered by crowdfunding to campaigners in Europe.

Large datasets about crowdfunding can be obtained by manually monitoring the existing platforms, the number of offered projects, the amounts raised, the number of projects per model, etc. Several commercial providers have started monitoring this data and sell reports and datasets or offer access to their datasets for a fee. Crowdfunding hotspots and selected other Member States should be monitored to assess the number of emerging platforms and the popularity of each model and to estimate the overall market size in Europe. When done regularly and systematically, trends of development can be seen over time, and provide an overview on the crowdfunding climate and economic impact per Member State.

The frequency of the benchmarking highly depends on the update intervals of the main sources. As crowdfunding is a fast developing market, it is recommended to perform the monitoring and benchmarking exercise at least bi-annually.

The table overleaf provides a first indicative list of elements that could be captured in a crowdfunding market report. The potential source and method of gathering the data has been partly outlined. As the EC is likely to be the main beneficiary initially, it could take a lead role in shaping such an instrument. Over time influential industrial players will realise the potential of officially compiled information and their possible contribution to mature the market further. Experience from other industries show, that market data, in this particular instance, the bottom-up platform statistics is most effectively fed in by industry itself. Therefore over time the production of this market report could potentially be entrusted to a European industry association which cooperates with the European Commission.

Key Points

- A scorecard for equity-based crowdfunding could help regulatory stakeholders to monitor the market development and potentially assess the impact of new regulations over time
- Four key groups of KPIs are proposed: the market demand, the maturity of the regulatory framework, the supply of intermediary services and the supply of capital
<table>
<thead>
<tr>
<th>Market indicators</th>
<th>Rationale</th>
<th>Potential source</th>
</tr>
</thead>
<tbody>
<tr>
<td>Crowdfunding awareness</td>
<td>Awareness of the general public about crowdfunding</td>
<td>Prevalence of news articles on the subject</td>
</tr>
<tr>
<td></td>
<td>Knowledge of the different crowdfunding instruments</td>
<td>Quantitative web survey</td>
</tr>
<tr>
<td>Start-up ecosystem</td>
<td>Indicator on entrepreneurial activity &amp; development</td>
<td>Data from governmental agencies</td>
</tr>
<tr>
<td></td>
<td>Need for finance in the seed stage</td>
<td>Global Entrepreneurship &amp; Development Index (GEDI) Index</td>
</tr>
<tr>
<td>Familiarity with e-commerce</td>
<td>Country’s openness and acceptance of e-commerce</td>
<td>Eurostat</td>
</tr>
<tr>
<td></td>
<td>% of GDP by e-commerce</td>
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<tr>
<td>...</td>
<td>Qualitative analysis of regulatory activities on crowdfunding</td>
<td>Interviews</td>
</tr>
<tr>
<td>N° of MS involved in crowdfunding</td>
<td>Governmental support of CF platforms / companies</td>
<td>Data from national governments</td>
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<tr>
<td></td>
<td>Implementation of government regulation</td>
<td>EBAN</td>
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<tr>
<td>Supply of intermediary services</td>
<td>Size per campaign sectors</td>
<td>Private market intelligence companies</td>
</tr>
<tr>
<td></td>
<td>Size and growth of market per MS</td>
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<tr>
<td></td>
<td>Size and growth of market per model</td>
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<tr>
<td>Market evolution</td>
<td>Evolution crowdfunding instruments</td>
<td>Desk research</td>
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<td>Number of platforms by model</td>
<td>Number of platforms per type of model</td>
<td>Interviews</td>
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<tr>
<td>Emergence of new platforms or consolidation trends</td>
<td>Market dynamics and maturity</td>
<td>Qualitative assessment of platform evolution</td>
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<td>Qualitative assessment of platform evolution</td>
<td>Interviews</td>
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<td>...</td>
<td>Volume of investment in the early stage</td>
<td>Investment Overview by EBAN</td>
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<tr>
<td>Volume &amp; average raised per model</td>
<td>Compare popularity of crowdfunding with BAs market volume</td>
<td>European Commission</td>
</tr>
<tr>
<td></td>
<td>Compare popularity of crowdfunding with VCs market volume</td>
<td>EVCA statistics</td>
</tr>
<tr>
<td>Global crowdfunding hotspots</td>
<td>Size and growth of market per MS</td>
<td>Private market intelligence companies</td>
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<td></td>
<td>Size and growth per model</td>
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<td></td>
<td>Ticket size campaign</td>
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<tr>
<td>Familiarity with e-commerce</td>
<td>Country’s openness and acceptance of e-commerce</td>
<td>Eurostat</td>
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<td>% of GDP by e-commerce</td>
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<td>...</td>
<td>Comparison of EU situation in global scale</td>
<td>Desk research</td>
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<td></td>
<td>Private market intelligence companies</td>
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</tr>
</tbody>
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Table 6: Proposed indicators for monitoring the crowdfunding ecosystem
5. Perspectives for an Evolving Regulatory Landscape

5.1. Towards regulatory concepts

Crowdfunding is a relatively recent phenomenon and as such only some regulatory efforts have been made specifically addressing this funding instrument in Member States. The current European regulatory framework already covers a variety of aspects of crowdfunding, with different implementations in each Member State. One of the objective of this study is to provide to the European Commission with a set of regulatory concepts on how the crowdfunding regulatory framework could be improved in order to stimulate the uptake of crowdfunding in Europe, whilst safeguarding the interests of the general public.

The approach followed to determine the initial regulatory concepts in this report, is based on a limited stakeholder consultation. Initial concepts for regulation has been
discussed with selected crowdfunding platforms, campaign backers, campaign owners, business angels, institutional investors and industry associations. Initially platform operators prefer the lightest form of regulation as they can focus on developing their offering and the market and are wary of the additional cost and resources needed to implement stricter regulation. The main concern of financial authorities on the other hand when adapting or implementing their adapted regulation, is to enhance investor protection besides providing a clear regulatory framework for platforms to operate under. It is therefore of utmost importance in this exercise to consult actors from within but also outside of the sector and to draw analogies with other financial service providers.

This report looks beyond government regulation and provides an initial assessment of the viability of several harmonisation concepts, detailed in the context of different scenarios. These scenarios can serve as a basis for policy makers to investigate the national regulatory framework and options in depth. It is clear for most of the stakeholders in the sector that some form of harmonisation and regulatory transparency is desired in order to protect the crowdfunding backers, campaigners and platforms and to stimulate industry to unlock the economic potential of the instrument. It should be noted that regulatory efforts are never “one-size-fits-all”, each Member State has its own priorities, traditions and legislation. Furthermore each crowdfunding model has its specificities and issues to be solved.

A variety of regulatory concepts exists, ranging from self-regulation to imposed government regulation, each with their own benefits and disadvantages:

<table>
<thead>
<tr>
<th>Monitoring mechanism</th>
<th>European Code of Conduct</th>
<th>European Quality Label</th>
<th>National Legislation</th>
<th>European Regulation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Platforms perform a self-assessment and vow to a set of standards/best-practices defined by the industry</td>
<td>A third-party performs the assessment of a platform’s compliance with standards and grants a quality label</td>
<td>National laws regulate the operations of the platform on a national level, protecting the backer</td>
<td>A balanced European regulation governing platform operations on a pan-European level</td>
<td></td>
</tr>
<tr>
<td>Definition of quality standards</td>
<td>Industry</td>
<td>Industry</td>
<td>Government</td>
<td>Institutions</td>
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<tr>
<td>Adherence</td>
<td>Optional</td>
<td>Optional</td>
<td>Mandatory</td>
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<tr>
<td>Impact on market development</td>
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<tr>
<td>Ease of implementation and operation</td>
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Figure 20: High-level spectrum of instruments in a crowdfunding regulatory framework
The European Commission has held a public consultation on crowdfunding in the EU at the end of 2013 and has subsequently published a communication on the topic. Several initiatives to support the uptake of the crowdfunding were defined and the EC has set the following priorities\textsuperscript{69} in the communication:

- An EU Expert Group on crowdfunding was established with stakeholders of the sector. The particular focus areas of the group are to explore the potential of a quality label and to provide expertise in promoting transparency, best practices and certification;
- Raising awareness with regards to crowdfunding, promoting information and training as well as raising standards;
- Mapping national regulatory developments and holding regulatory workshops to ensure an optimal functioning of the internal market, and to assess if regulatory intervention is necessary at EU level.

In addition, the European Securities and Markets Authority (ESMA) and the European Banking Authority (EBA) performed a consultation with the national authorities in 2013 to better understand the current national regulatory frameworks for crowdfunding.

\textbf{Key Points}

- The EU institutions are taking various steps to support the development of crowdfunding whilst safeguarding the interests of retail investors
- Stakeholders from within and outside the crowdfunding sector have shared their views on various regulatory concepts
- An improved regulatory framework would be beneficial to all stakeholders. Four regulatory concepts have been outlined

\textsuperscript{69} European Commission, COM(2014)172, Unleashing the potential of crowdfunding in the EU, 2014
5.2. Non-financial models require limited regulatory action

The non-financial crowdfunding platforms exist for more than 5 years and there is only little anecdotal evidence of abuse or fraud on these platforms. This type of crowdfunding is believed to be inherently self-regulating by the characteristics and mechanisms of the model itself. Firstly, the campaigns are evaluated by a large number of people, crowdsourcing the decision on whether or not the campaign is credible and viable. Whilst it may be possible that a few people are tricked into funding a fraudulent campaign, the wisdom of the crowd dramatically reduces this risk. Secondly, the relatively short lead-time between the funding of a campaign and the outcome of the campaign (i.e. visibility on the use of the funds by the campaign owners or the receipt of the promised reward) provides a rapid assessment of the individual campaign and on the trustworthiness of the mechanism in general and. Thirdly, the social element of crowdfunding allows negative feedback to be rapidly disseminated within the community and beyond, and ensures the campaigners are under pressure to fulfil their obligations. In conclusion, this model is effectively regulated by the inherent principles of democracy and social control, as demonstrated by the very limited cases of abuse.

Whilst crowdfunding campaigns often deliver their rewards later than promised, in the case of complete failure of delivery, the current regulatory framework, for example the consumer protection rules, are deemed sufficient to cover this risk and provide the campaign backers with sufficient tools to protect themselves from abuse or fraud. In case the company is based outside of the EU, taking action against the campaign owner may be legally and financially burdensome, a risk that campaign backers should take into account. Furthermore, in case of the pre-selling model, when the campaign backer orders products that are still in various stages of development, campaign backers should evaluate this risk properly before committing their funds. The crowdfunding platforms typically do not accept any responsibility in case of failure and generally only verify whether a proposed campaign fulfils the platforms’ eligibility criteria. Some platforms have started to conduct identity checks on campaign owner to reduce the risk of fraud.

The different identified scenarios – to be analysed in further depth by policy-makers with regards to their advantages, disadvantages and impact – are summarised hereafter.
**Scenario 1: No market intervention**

Up to now, no systemic evidence of abuse or fraud on the crowdfunding platforms has emerged. The current crowdfunding market appears to be sufficiently self-regulated; to the contrary, the market is thriving and thus indicating trust between all parties involved.

**Scenario 2: Code of Conduct**

A system of self-regulation in the crowdfunding sector could further strengthen trust between platforms, campaign backers and campaign owners. A unified code of conduct could be developed in Europe, supporting the further uptake of crowdfunding, especially beneficial for Member States without an adapted crowdfunding regulation or Member States where doubts about online transactions prevail and where crowdfunding is developing at a slower pace. In the context of this report, *a code of conduct is defined as a self-assessment by platforms which vow upon acceding to a set of minimum standards and best practices*. The code of conduct could be developed by either the industry itself, in the frame of a European industry association, or could be a concerted effort between industry and national / European institutions. The benefit of a European code of conduct versus a national code is that it pre-emptively addresses the cross-border nature of donation/reward/pre-selling-based crowdfunding and enhances the recognition of the code amongst campaign backers. A code of conduct, within the definition of this report, would not entail a frequent monitoring to ensure compliance of the platform, as it is unlikely that the emerging industry associations would be willing to take on this demanding task (platforms are emerging at a rapid pace) and since most of the platforms would already be largely compliant or it would require minimal resources to become compliant. The code of conduct would, however, spark a discussion within the industry on how to enhance its services and protect its consumers to their best ability; whilst building trust with campaign backers regarding this new funding instrument.

A code of conduct could self-regulate the following topics:

- **Transparency**: provide clear, easy-to-access and understandable information on the crowdfunding process (campaign selection, fundraising process and campaign’s monitoring post-funding), the associated risks and the liabilities of the involved parties, especially in case the campaign fails to deliver on its promises; make accessible all contractual terms between the platform, the campaign owners and backers before the actual commitment of funds by the backers, ensure contracts are understandable and in layman’s terms;
- **Good business conduct**: ensure contracts are balanced between parties and offer sufficient legal protection to the campaign backers; ensure that the funds committed by campaign backers are sufficiently protected and ring-fenced from the platform’s own funds;

- **Privacy & security**: protect the personal information provided by the campaign backers and campaign owners.

For instance, the UK Crowdfunding Association has developed a Code of Practice to which its members are obliged to subscribe. The European Crowdfunding Network has also developed a Code of Conduct for its members to adhere to, however, the Code of Conduct is relatively vague and seems to have as objective to address the operations of the network rather than specifically the operations of its members’ platform. A European effort could be set-up, governed by an industry association or within the expert group of the European Commission.

**Scenario 3: National or European regulation**

In case of wide-spread abuse or fraud in the future, the national authorities or the European institutions could contemplate governing the non-financial return models under a national or European regulation or a directive. The legislation could set in stone the best practices for the platforms’ transparency and good conduct. It should be noted, however, that many of the practices are already governed by existing legislation. One of the possibilities to ensure compliance under this legislation could involve the set-up of a license which platforms need to obtain. The European regulatory process is lengthy and involves consultation with many stakeholders, and, in the case of a Directive, an implementation process on national level. As such, crowdfunding legislation is likely to remain behind the latest market developments. Furthermore, there is the risk that national governments would push for their interpretations to be reflected in a European framework, thus making it both complicated and difficult to implement. This scenario would likely be a means of last resort, to be considered in case other mechanism do not provide a satisfactory outcome and would need to be sufficiently assessed in terms of expected impact.

**Key Points**

- Limited evidence of fraud or abuse is known for the non-financial return models
- Non-financial crowdfunding platforms generally provide sufficient transparency for both the campaign backer and the campaigner
- For non-financial return models a code of conduct could further enhance transparency and build trust between investor, investee and crowdfunding platform
5.3. Regulatory concepts for equity-based crowdfunding

The rapid emergence of equity-based crowdfunding platforms, has taken national authorities somewhat by surprise. The existing national regulations are not always conducive to the operation of equity-based crowdfunding platforms and investment by campaign backers. New specific regulations and guidelines for crowdfunding by the national authorities are (justly or unjustly) being criticised by industry stakeholders, but always intend to add an additional layer of protection for the retail investors. The FCA’s guidelines regarding crowdfunding in the United Kingdom for instance, were initially met with certain scepticism (especially the required license to operate was deemed to be to resource and time-consuming to obtain), but are today generally appreciated by industry stakeholders for the level of protection that they provide to the investors (e.g. by introducing investment caps and by the requirement to provide risk warning systematically). There are many complexities and hurdles for crowdfunding platforms to overcome, especially when wishing to operate on a pan-European level, whilst simultaneously offering sufficient protection to investors. A concerted effort by all involved parties – the crowdfunding platforms, national authorities and European legislators – could stimulate the uptake of this model of crowdfunding in Europe. At the moment, Europe has a more lenient legislation in terms of equity crowdfunding compared to e.g., the United States, but as described earlier in the report other regions are also progressing on legislative efforts. A balance between regulation to protect the retail investor and flexibility for platforms to operate has to be sought. The current regulatory framework in Europe appears to pose fewer issues for the lending-based platforms than for securities platforms.

Two key issues in the industry have been identified. They highlight a clear need for evolution of the regulatory framework, namely a lack of transparency and a lack of harmonisation.

As described in this report, there exists a variety of models of equity-based crowdfunding is large and the differences are complex to understand. In itself this should not be an insuperable issue, but a lack of transparency and education for both potential investees and investors render this situation somewhat precarious. In many instances, both investor and investee remains insufficiently informed about:

- The real risk of investing in start-up companies, probabilities of success, exit uncertainty due to potential lack of a secondary market for the securities obtained; or the legally forbidden sale of the obtained securities or contracts;
- The exact legal instrument that is being bought: straight equity, a stake in an intermediate holding company or an equity-like contract;
- The holder of the legal title to the shares of the company: the investor directly himself, a nominee, an intermediate holding company or no-one;
- Visibility on all contracts between the intermediate holding company or nominee and the investee;
- The nature of voting rights, if any;
- The contractual conditions or shareholder agreement for exit or follow-on financing (dilation, drag-and-tag clauses, etc.) both for the investor as investee;
- The legal rights in case the investee fails (preferential shares vs. common shares; junior debt vs. normal debt); or in case of a lack of follow-on financing;
- The total costs (one-off fee or management fee to intermediate holding company or nominee);
- The mechanisms to ring-fence campaign funds from platforms’ own finances.

It should be noted that crowdfunding platforms mention some of the above details in the support section or terms of use on their website. Further information can be retrieved in the contracts investees agree to at the moment they decide to invest, however, a complete view on the above information can rarely be found beforehand and is seldom explained in laymen’s terms. As the majority of the crowdfunding platforms market their campaigns to the general public, it is crucial for consumer protection that the above information can easily be retrieved.

A second key issue are the diverse national regulatory frameworks in Europe. Many platforms are avoiding the stricter regulations under their national legislation, resulting in a plethora of crowdfunding types in the equity-based model in the Member States. In order to ensure fair competition between platforms and to enhance transparency for the retail investors, harmonisation of national regulation could be pursued. Legal uncertainty could potentially harm the industry in some Member States. The European regulatory framework provides a sufficient legal basis for national regulators to implement rules that could allow both the platforms to operate in a workable legal framework, as to protect the investor and investee. The national authorities bear the responsibility of acting, since they have the instruments at hand to implement and harmonise balanced rules for crowdfunding in the near term.
Scenario 1: No market intervention

National authorities possess the necessary tools to enable equity-based crowdfunding on a European scale, based on existing European legislation. It could be argued that the market will develop itself, pushing the regulatory framework where necessary. Nevertheless, it could be contended that different national regulations might independently develop without a pan-European view on the development of equity-based crowdfunding. Furthermore, the transparency issue (caused by different legal systems and hence different financial instruments in each Member State) is unlikely to be resolved without any intervention through self-regulation or government legislation, resulting in insufficient protection for the crowdfunding investors.

Scenario 2: Quality label

To professionalise the equity-based crowdfunding industry on a European level, a quality label could be considered which should address three main topics: increase transparency, ensure implementation of best practices and contribute to education. In the context of this report, a quality label is defined as a label granted to a platform by a third party after this third-party performs an assessment of the platform’s compliance with a set of minimum standards or best practices. A pan-European industry association in cooperation with national associations could govern the quality label’s processes, ensuring the proper implementation of, and the continued monitoring of compliance with, the requirements for obtaining the quality label. Monitoring of the compliance of the platform should be conducted potentially leveraging the inherent crowd/peer pressure in this highly dynamic industry. It remains to be seen whether industry associations can cover the associated costs with member fees (some financial support in the form of a grant could be considered, as detailed in scenario 3) and whether platforms themselves would be willing to engage on the certification process.

The required minimum standards or best practices for obtaining the quality label should be the subject of discussion with all stakeholders (e.g. led by industry but including as well authorities, consumer groups and traditional finance actors) with a view to protect everyone’s interests. It should be noted that the European Commission has recently established an Expert Group on crowdfunding which has been tasked to discuss such a quality label, the outcome of this group could serve as valuable input for the industry to act upon.
An initial topic which could be addressed by a quality label is the *transparency* issue. In addition to the code of conduct topics for the non-financial models, the following items could be additionally addressed by the quality label. First, to improve transparency, a Europe-wide standardised platform or campaign identity card could be implemented, highlighting in laymen’s terms the key characteristics and mechanisms of the financial instrument(s) used by the equity-based crowdfunding platform. This identity card should be easily accessible without having to commit to an investment and potentially without even having to register on the platform. Secondly, risk warnings in all communication channels of the platforms could aid the retail investors to make informed decisions. Lastly, all contractual documents between the platform and investee, and between the platform and the investor could be made available on the platform’s website, well before the actual investment decision has been made by the campaign backer (rather than at the moment the campaign backer starts the investment process on the platform).

Similar to the proposed code of conduct for the non-financial return models, the *good business conduct* guidelines could govern best practices in relation to the set-up of contracts in order to both protect the investor and investee, especially in the case of follow-on financing or exit; but also in relation to the management of the investors’ funds; the background checks performed on investee, the verification of investment-savviness, identity checks on investors; etc.

Lastly, it would become the responsibility of the equity-based platform to educate customers on the financial instruments they use. Whilst the general public might be interested in financially supporting innovative companies, they should be informed about the different types of crowdfunding models and what the advantages and implications of such an investment are.

As an alternative to a quality label, a code of conduct could be implemented demanding that platforms fulfil a similar set of requirements. Without a certification body verifying the implementation of the code of conduct principles, the envisaged outcome will probably not be obtained in full. The principles outlined above would require more substantial efforts from the equity-based crowdfunding platforms than in is the case for the non-financial return models and as such, a quality label would be preferable to ensure compliance.
Scenario 3: Harmonisation of national regulation

Equity-based crowdfunding activities typically face a combination of different regulations amongst which regulations on financial promotions for the individual campaigns and good conduct regulations on financial activities and transactions for the platform operators. While different regulations impact crowdfunding operations, and the national interpretations of harmonised rules differ in each Member State, there is sufficient room for platforms to operate. Member States regulators gradually improve their understanding of equity-based crowdfunding, and consequently, more specific rules and guidelines are established. This creates more legal certainty for the platform operators, but also a higher level of protection for the users. Under the welfare state principles, retail investors are offered statutory protection against exposure to high-risk investments. Crowdfunding-specific rules try to offer this protection through a number of measures. One mechanism that is becoming increasingly popular - as applied in the British and Spanish legal initiatives - is to cap the contributions that users can make to an individual campaign or to investment crowdfunding in general. New regulations tend to generate rather critical responses from the industry, but the case of the United Kingdom – which is now seen as one of the more exemplary regulations – proves that the development of the sector can go hand-in-hand with sufficient investor protection.

The current European regulatory framework itself is deemed to provide sufficient regulatory instruments to national authorities to accommodate all types of crowdfunding. In order to achieve a certain level of regulatory harmonisation in Europe, however, it could be necessary to activate the Member States. In the case of equity-based crowdfunding, the authors of this report would propose to take the route of a European equity crowdfunding industry association that interacts with national policy-makers and authorities in order to improve the regulatory framework as the industry matures.

An analogy could be drawn with the European Private Equity & Venture Capital Association (EVCA), which was created under stimulus of the European Commission in 1983. The EVCA represents and promotes the European private equity and venture capital industry. The association’s objectives include the education of its stakeholders, providing research on the sector, shaping public policy and stimulating good business conduct amongst its members. The association is highly valued and well respected for its efforts in the legislative process and could serve as an example for a pan-European industry association for each type of crowdfunding.
A strong European equity crowdfunding industry association could be stimulated through an open call in Horizon 2020, as member fees might currently not provide the required revenue stream to operate professionally. It is recommended that the open call would seek proposals fulfilling following criteria: proven experience in influencing the national legislative process, confirmed support of key industry players and national industry associations, proven insight into the underlying issues in the industry from a regulatory and ethical point-of-view, intention to support a balanced regulatory path for both the platforms, retail investors and investees and insight into the best practices for platform operations.

The European Commission together with a well-equipped European equity crowdfunding industry association could potentially prepare guidelines with practical recommendations for the national authorities on how to implement equity-based crowdfunding rules in their national regulations, with reference to existing broader regulation, in order to protect the retail investor and investee, and to maintain a workable regulatory regime for the equity-based crowdfunding platforms to emerge and operate on a pan-European scale. An incentive for Member States could be the increased attraction of foreign investors on the national platforms if they are adequately structured and the economic growth this could bring.

National authorities could investigate whether it makes sense to require platforms to obtain licenses to operate or not. Platforms argue this procedure is lengthy and costly, but on the other hand, a certain caution and seriousness should be displayed when becoming an intermediary of financial products to the general public. Regulatory authorities should bear in mind, however, that requesting equity-based crowdfunding platforms to obtain a license in each Member State in which they plan to operate is cumbersome and will not support the emergence of pan-European equity-based crowdfunding platforms, limiting access to finance for their national start-up communities.

**Scenario 4: European regulation**

As a means of last resort, in case the other regulatory scenarios insufficiently address the issues at hand, the European Commission could evaluate the preparation of a European regulation or directive specifically addressing equity-based crowdfunding, or to include crowdfunding in other Directives such as MiFID. In order to harmonise the regulatory framework in Europe, a regulation would have preference from a legislative point-of-view, as it would override the existing national laws with immediate effect.
and it leaves no room for different interpretations and implementations in each Member State, as it is the case for a Directive.

An equity-based Crowdfunding Regulation could harmonise the rules regarding the requirement to issue a prospectus, requirements to obtain a license from national authorities, and could define the limits for how much a company may raise from the general public per year and how much an individual investor may invest per year. In addition, the investor protection could be enhanced by enforcing sufficient risk warnings when communicating with retail investors.

It should be noted that this route requires a substantial effort and is naturally a rather lengthy process. Whilst equity-based crowdfunding is not as complex as other financial instruments regulated by European Directives, an analogy could be drawn to the AIFMD that came into force in 2013. The preparation of the AIFMD took several years, and involved many consultations and negotiations with industry and Member States. Due to the different perspectives and interests of the Member States, the view has been expressed by industry that the Directive has become too restrictive. In order to properly address the issues of equity-based crowdfunding, these two caveats of the European legislative process should be ideally avoided in the case of crowdfunding.

<table>
<thead>
<tr>
<th>Key Points</th>
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<tbody>
<tr>
<td>In Member States with a developing equity-based crowdfunding market, regulatory initiatives are in place or underway. A disparity exists between the different national solutions</td>
</tr>
<tr>
<td>A quality label could serve as an effective solution to address some issues with financial models and improve investor protection</td>
</tr>
<tr>
<td>The EU could be instrumental in providing a forum for all actors in order to enhance transparency for the investor</td>
</tr>
<tr>
<td>The growth of the market could be spurred by a cross-border harmonisation effort, potentially driven by European Industry Associations and national authorities</td>
</tr>
</tbody>
</table>
ANNEX 1 – LEADING EQUITY PLATFORMS IN EUROPE

Sources

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Crowdcube (UK)  Archive.org, own website
## ANNEX 2 – SUMMARY TABLE OF APPLICABLE REGULATION

<table>
<thead>
<tr>
<th>Country</th>
<th>Prospectus Limited</th>
<th>Requirements for Licence of Financial Authorities</th>
<th>Limits for Investors</th>
<th>Other</th>
</tr>
</thead>
<tbody>
<tr>
<td>FR</td>
<td>EUR 1 Million</td>
<td>AMF (Regulation: Ordonnance n° 2014-559)</td>
<td>≤EUR 1 K (for crowdlending only)</td>
<td></td>
</tr>
<tr>
<td>DE</td>
<td>EUR 1 Million (under new proposed regulation), but information document required</td>
<td>BaFin</td>
<td>≤EUR 10 K (under new proposed regulation)</td>
<td>Staff needs to demonstrate relevant skills; platforms need to produce an information document if they accept contributions more than EUR 250 (under new proposed regulation)</td>
</tr>
<tr>
<td>UK</td>
<td>EUR 5 Million per issuer within 12 months</td>
<td>FCA</td>
<td>≤10% of net assets per year</td>
<td></td>
</tr>
<tr>
<td>ES</td>
<td>EUR 5 Million per issuer within 12 months</td>
<td>No</td>
<td>≤EUR 3 K per project ≤EUR 10 K in a platform (During a 12-month period)</td>
<td>Legal initiative propose: stricter regime should apply including accounting and auditing</td>
</tr>
<tr>
<td>IT</td>
<td>EUR 5 Million per issuer within 12 months</td>
<td>Only for professional online portal manager; if the portal manager is a financial intermediary no licence is required and the enrolment in the Consob register is automatic</td>
<td>5% of the equity offer should be taken by professional investors before offer completion</td>
<td>Under a Italian specific &quot;crowdfunding law&quot; Payment requires to be licensed by Bank of Italy</td>
</tr>
<tr>
<td>SE</td>
<td>EUR 1.5 Million within months</td>
<td>S-FSA or cooperation with licensed firm</td>
<td>Possible to offer investments in limited liability companies formed as “private”, with limitations on the number of investors</td>
<td>Require a license when securities or investment products are sold; payment requires to be licensed by S-FSA</td>
</tr>
<tr>
<td>FI</td>
<td>EUR 1.5 Million per 12 months</td>
<td>No</td>
<td>No</td>
<td>Finnish Credit Institutions Act and Investment Services Act</td>
</tr>
<tr>
<td>SK</td>
<td>EUR 100 K in EU within 12 months</td>
<td>NBS</td>
<td>No</td>
<td>Financial Instruments Market Act; Payment Services and Systems Act</td>
</tr>
<tr>
<td>BG</td>
<td>EUR 100 K within 12 months</td>
<td>Bulgarian National Bank</td>
<td>No</td>
<td>Law on Credit Institutions &amp; Law on Payment Services and Payment Systems</td>
</tr>
<tr>
<td>PL</td>
<td>EUR 5 Million per issuer within 12 months</td>
<td>No</td>
<td>No</td>
<td>National Law</td>
</tr>
<tr>
<td>Country</td>
<td>Securities USD 1 Million (EUR 750 K) per 12 months</td>
<td>SEC, register as a broker or crowdfunding platform</td>
<td>USD 2 K (EUR 1.5 K) or 5 % of annual income for net worth less than USD 100K (EUR 75 K) per year; 10 % of annual income for net worth more than USD 100K (EUR 75 K) per year</td>
<td>Corporations and Market Advisory Committee legal regulation</td>
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</tr>
<tr>
<td>US</td>
<td>AUD 5 Million (EUR 3.5 Million) per year</td>
<td>No</td>
<td>AUD 2.5 K (EUR 1.8 K) per issuer; AUD 10 K (EUR 7 K) in total per year</td>
<td>Corporations and Market Advisory Committee legal regulation</td>
</tr>
<tr>
<td>AU</td>
<td>JPY 100 Million (EUR 730 K) per campaign</td>
<td>No</td>
<td>JPY 500K (EUR 3.7 K) per investor</td>
<td>Under new proposed regulation, will come into effect in May 2015</td>
</tr>
<tr>
<td>JP</td>
<td>SGD 5 Million (EUR 3 Million) in a year</td>
<td>No</td>
<td>No</td>
<td>Singaporean Securities and Futures Act</td>
</tr>
<tr>
<td>SG</td>
<td>USD 500 K per year</td>
<td>No</td>
<td>USD 10 K per issuer for start-up; USD 10 K per issuer for Individual issuer</td>
<td>Capital Market Act Start-up Companies Support Act</td>
</tr>
<tr>
<td>KR</td>
<td></td>
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